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BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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

2006 JUL -7 P 3: 03
AZ CORP COMMISSION
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ARIZONA WATER COMPANY, an Arizona corporation,
Complainant,

vs.

GLOBAL WATER RESOURCES, LLC, a foreign limited liability company; GLOBAL WATER RESOURCES, INC., a Delaware corporation; GLOBAL WATER MANAGEMENT, LLC, a foreign limited liability company; SANTA CRUZ WATER COMPANY, LLC, an Arizona limited liability corporation; PALO VERDE UTILITIES COMPANY, LLC, an Arizona limited liability corporation; GLOBAL WATER – SANTA CRUZ WATER COMPANY, an Arizona corporation; GLOBAL WATER – PALO VERDE UTILITIES COMPANY, an Arizona corporation; JOHN AND JANE DOES 1-20; ABC ENTITIES I – XX,

Respondents.

DOCKET NO. W-01445A-06-0200
SW-20445A-06-0200
W-20446A-06-0200
W-03576A-06-0200
SW-03575A-06-0200

Arizona Corporation Commission
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Global's Supplemental Brief

Regarding Preliminary Injunction

At the conclusion of the June 15, 2006 procedural conference in this case, the Administrative Law Judge requested that the parties file supplemental briefs by July 7, 2007. The briefs were to address the Commission's authority to impose a preliminary injunction banning respondents from entering into Infrastructure Coordination and Financing Agreements ("ICFAs") while this case is pending. Accordingly, respondents (collectively, "Global") file their supplemental brief.

1 **I. Preliminary Statement.**

2 Arizona courts recognize that before a state agency can enter an order depriving a person of
3 a property or liberty interest, due process requires the agency to provide notice and a hearing.
4 Accordingly, the Commission cannot adopt a preliminary injunction without conducting a hearing.
5 In this case, conducting a hearing would be impractical, as the substantive matters at issue here are
6 being resolved in the generic financing proceeding, docket no. W-00000C-06-0149. Accordingly,
7 the Commission should not conduct a hearing, and thus, it should not issue a preliminary
8 injunction.

9 If the Commission does conduct a hearing, it should apply the traditional four part test for
10 preliminary injunctions. This test looks to likelihood of success, irreparable harm, balance of
11 harms, and the public interest. These factors do not support issuing a preliminary injunction in this
12 case. Indeed, the determination of a likelihood of success will be directly affected by the generic
13 financing proceeding.

14 Moreover, under Arizona law, a preliminary injunction can be granted only upon a
15 showing based on sworn evidence in the form of affidavits or a verified complaint. Here, there is
16 no sworn evidence in the record, and thus an injunction cannot be issued at this time.

17 Lastly, an injunction can be issued only when the tribunal has jurisdiction. Here, the
18 Commission does not have jurisdiction over a number of the respondents. These non-
19 jurisdictional respondents include the respondent that actually enters into the ICFAs. Because the
20 Commission does not have jurisdiction over that respondent, the Commission cannot adopt a
21 preliminary injunction banning it from entering into ICFAs.

22 **II. Arizona administrative agencies must conduct a hearing before adopting provisional**
23 **or preliminary remedies.**

24 Under Arizona law, an administrative agency may not affect liberty or property interests
25 without conducting a hearing prior to granting any preliminary remedy. The leading case is *Webb*
26 *v. State ex rel. Arizona Bd. of Medical Examiners*, 202 Ariz. 555, 558, 48 P.3d 505, 509 (App.
27 2002). In that case, the Board of Medical Examiners conducted a hearing where a doctor could

1 have been reprimanded, censured, or had his license temporarily suspended. The court ruled that a
2 “person facing such a range of consequences... must at a minimum be provided a chance to
3 confront adverse evidence and question adverse witnesses.” *Id.* Another example is *Dahnad v.*
4 *Buttrick*, 201 Ariz. 394, 399, 36 P.3d 742, 747 (App. 2001). In that case, the Board of Dental
5 Examiners, without holding a hearing, suspended a dentist’s license until the conclusion of the
6 case. The court overturned this action, finding that it violated the dentist’s due process. The court
7 recognized an exception where “emergency circumstances imperatively require such action” to the
8 general rule requiring a hearing. *Id.* Even under this emergency exception, the agency must
9 provide a “prompt or immediate” hearing after issuing the emergency order. *Id.* Here, there has
10 been no allegation of emergency, nor is there any basis for such an allegation, and accordingly a
11 hearing is required.

12 Moreover, this Commission has no procedural rule governing preliminary injunctions or
13 other provisional remedies. In the absence of a procedural rule, the Commission has determined
14 that the Rules of Civil Procedure should apply. A.A.C. R14-3-101(A). Under the Arizona Rules
15 of Civil Procedure, a court cannot issue a preliminary injunction without the opportunity for a
16 hearing. *See McCarthy Western Constructors, Inc. v. The Phoenix Resort Corp.*, 169 Ariz. 520,
17 525, 821 P.2d 181, 186 (App. 1991). In addition, the rules require that the court issue findings of
18 fact based on the evidence heard. *Id.*

19 Although a hearing is required, it would not be practical to conduct a hearing at this time.
20 During the procedural conference, the Administrative Law Judge indicated that this case would be
21 stayed until there is a determination in the generic financing docket. That docket is proceeding
22 rapidly, and may very well be concluded before a preliminary injunction hearing could be
23 scheduled. In addition, conducting a hearing in this matter would not serve judicial economy
24 when these matters are already being reviewed in the generic docket.

25 For these reasons, it would not be practical to conduct a hearing at this time. And in the
26 absence of a hearing, the Commission may not issue a preliminary injunction or similar remedy.

27

1 **III. This case does not meet the traditional four part test for preliminary injunctions.**

2 As noted above, the Commission does not have a rule governing preliminary injunctions.
3 In the absence of any rule or established standard governing such proceedings, the Commission
4 should look to the traditional four part test governing preliminary injunctions. The Arizona
5 Supreme Court recently repeated the traditional test as:

- 6 1. a strong likelihood of success on the merits;
- 7 2. irreparable harm if the stay is not granted;
- 8 3. that the harm to the requesting party outweighs the harm to the party opposing the
9 stay; and
- 10 4. that public policy favors the granting of the stay.

11 *See Smith v. Arizona Citizens Clean Elections Commission*, 212 Ariz. 407, ¶ 10, 132 P.3d 1187,
12 1190-91 (2006)(adopting preliminary injunction test as test for stay on appeal); *see also Shoen v.*
13 *Shoen*, 167 Ariz. 58, 63, 804 P.2d 787, 792 (App. 1991)(reciting traditional four part test). This
14 test is not satisfied here.

15 The first prong is whether there is a strong likelihood of success on the merits. Global has
16 reviewed the legal and factual issues regarding this case in its Motion to Dismiss and Reply in
17 Support of Motion to Dismiss. For the reasons stated in those documents, AWC does not have a
18 strong likelihood of success. Moreover, the determination of a likelihood of success should not be
19 made until the Commission resolves key policy and legal issues in the generic docket.

20 The second prong is irreparable harm. For harm to be “irreparable”, the inquiry “must be
21 both certain and great; it must be actual and not theoretical.” *Wisconsin Gas v. F.E.R.C.*, 758 F.2d
22 669, 674 (D.C. Cir. 1985). Thus, speculative harms related to regulatory policy do not qualify as
23 irreparable. *See Id.* As explained in the Motion to Dismiss, the ICFAs do not cause any harm at
24 all. Even if any harm did exist, it would certainly not be “irreparable.” The Commission remains
25 firmly in control of the CC&N process. No territory will be granted to Global in the absence of
26 Commission action through a CC&N. Moreover, the Commission will closely examine the ICFAs
27

1 in the generic docket, and it will have the opportunity in that docket to address any “harms”,
2 whatever those may be.

3 The third prong goes to a balancing of harms to the parties. In this case, AWC’s objections
4 to the ICFAs are generalized concerns that do not directly affect AWC. AWC has shown no harm
5 to itself. Moreover, even if AWC was being harmed, the duration of the harm would be short,
6 because the generic docket is proceeding quickly. Thus any harm to AWC would be minimal. In
7 contrast, a preliminary injunction would seriously harm Global. The ICFAs are at the heart of
8 Global’s strategy. This strategy is based on the “3Cs”: conservation, consolidation, and
9 cooperation. This strategy is explained in Global’s Comments in the generic docket (attached as
10 Exhibit A). As shown in the comments, the ICFAs enable Global to promote conservation of
11 limited groundwater resources, consolidation of troubled water companies, and cooperation with
12 cities and others. Without the ICFAs, Global’s ability to achieve these goals would be seriously
13 compromised. Global enters into ICFAs on a regular basis, and its everyday actions would be
14 sharply affected if a preliminary injunction is issued. In sum, a ban on ICFAs would harm Global,
15 but the absence of a ban would not harm AWC. Thus, this prong strongly points against granting a
16 preliminary injunction.

17 The fourth factor is the public policy or the public interest. As shown in the attached
18 comments, the ICFAs are used to promote goals that are in the public interest, such as
19 conservation, consolidation, and cooperation.

20 All four prongs of the test point against granting a preliminary injunction. In addition, no
21 injunction can be issued where there is an adequate remedy at law. *See The Power P.E.O., Inc. v.*
22 *Employees Insurance of Wausau*, 201 Ariz. 559, 562, 38 P.3d 1224, 1227 (App. 2002). Here,
23 AWC has not explained why a remedy in the generic docket would be inadequate. Moreover, an
24 injunction remains an extraordinary remedy. *See United States v. Oakland Cannabis Buyers’*
25 *Cooperative*, 532 U.S. 483, 496 (2001); *Mason Dry Goods v. Ackel*, 30 Ariz. 7, 13, 243 P. 606,
26 608 (1926). As such, it should be used sparingly and with great caution. There are no grounds for
27 imposing such an extraordinary remedy in this case.

1 **IV. Sworn evidence is needed before an injunction can be issued.**

2 Under Arizona law, an injunction can be issued only if it is based upon sworn evidence.
3 Under A.R.S. § 12-1803, an injunction can be granted before final judgment only if injunction is
4 supported by affidavits or a verified complaint.¹ Here, AWC's complaint was not verified and
5 AWC did not submit any affidavits in support of its request for an injunction. Accordingly, an
6 injunction cannot be issued at this time.

7 **V. The Commission does not have jurisdiction over Global Parent.**

8 Global Water Resources, LLC ("Global Parent") is the respondent that is the party to the
9 ICFAs. Global Parent does not provide water or wastewater service, and therefore it does not meet
10 the definition of a public service corporation in the Arizona Constitution. *See* Ariz. Const. Art.
11 XV § 2. There is no factual dispute on this point. As more fully explained in the Motion to
12 Dismiss and Reply, a company that does not meet this definition cannot be a public service
13 corporation. AWC suggests that the Commission can ignore the constitutional definition and
14 instead skip ahead and apply the so-called *Serv-Yu* test. Even if this were correct, by AWC's
15 admission, the *Serv-Yu* test is a "fact-intensive inquiry".² Since the question is so fact-intensive, it
16 is not an appropriate question to be resolved at this preliminary stage of the proceedings. Thus,
17 under AWC's own analysis, the Commission cannot determine at this time that it has jurisdiction
18 over Global Parent. And the Commission cannot act in the absence of jurisdiction, and any action
19 that it did take would be void. *See Tucson Rapid Transit Co. v. Old Pueblo Transit Co.*, 79 Ariz.
20 327, 289 P.2d 406 (1955).

21 **VI. Conclusion.**

22 The extraordinary remedy of an preliminary injunction should not be adopted in this case.
23 There has been no hearing as required by Arizona law and due process. The traditional four-factor
24 test for preliminary injunctions has not been satisfied, and in any event, AWC has not complied
25

26 ¹ This statute does not eliminate the requirement for a hearing for preliminary injunctions.
27 *See Nu-Tred Co. v. Dunlop Tire and Rubber Corp.*, 118 Ariz. 417, 419, 577 P.2d 268, 270 (1978).

² AWC Response to Global's Motion to Dismiss at 7:14.

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1 with the statutory requirements for an injunction. In addition, the Commission does not have
2 jurisdiction over Global Parent, and therefore cannot grant an injunction against it. For these
3 reasons, the Commission should decline to issue a preliminary injunction.

4 RESPECTFULLY SUBMITTED this 7th day of July 2006.

5
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7
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EXHIBIT

"A"

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

AZ CORP COMMISSION
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2006 JUN 23 P 4: 23

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8 IN THE MATTER OF THE COMMISSION'S
9 GENERIC EVALUATION OF THE
10 REGULATORY IMPACT FROM THE USE OF
11 NON-TRADITIONAL FINANCING
12 ARRANGEMENTS BY WATER UTILITIES AND
13 THEIR AFFILIATES

Docket No. W-00000C-06-0149

Global's Comments

14 Santa Cruz Water Company, LLC; Palo Verde Utilities Company, LLC; Global Water –
15 Santa Cruz Water Company; Global Water – Palo Verde Utilities Company; Cave Creek Water
16 Company; and Hassayampa Utility Company (the “Global Utilities”) and Global Water Resources,
17 LLC (“Global Parent”)(collectively “Global”) hereby provide their comments regarding this
18 docket.

19 **I. Introduction.**

20 We appreciate the opportunity to provide comments concerning the important subject of
21 non-traditional financing arrangements. Arizona has rapid growth combined with limited water
22 resources. We have carefully analyzed the issues facing our State – the Colorado River is,
23 according to ADWR, overallocated by millions of acre-feet per year, Arizona is in a very long
24 drought period, ADWR has been stymied by litigation in its efforts to enact meaningful gallons per
25 capita per day regulations, and the twin pressures of growth and arsenic compliance are
26 overwhelming small water companies. In this situation, it is essential that we find ways to
27 maximize the use of our water resources, while minimizing any potential adverse environmental
effects. Growth, arsenic compliance and the drought have stretched – sometimes beyond the
breaking point – the resources of small water and wastewater providers. These small utilities often

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1 lack the financial strength, management capabilities and technical expertise to keep up. And
2 growth all-too-often causes cities, utilities, and residents to squabble as they try to cope with
3 scarcity and increasing costs. These challenges require creative solutions. Non-traditional
4 financing arrangements can play an important role in alleviating these problems. Global Parent
5 welcomes the opportunity to explain how its Infrastructure Coordination and Financing
6 Agreements (“ICFAs”) can help solve these problems.

7 The ICFAs allow Global to implement the “3Cs”: conservation, consolidation, and
8 cooperation. Global believes that the 3C strategy is in the public interest, and that its
9 implementation – by Global and other companies – is critical to the future of our state. The 3Cs
10 can be summarized as:

11 **Conservation.** In a desert, water should not be squandered. As a state, we can – and
12 should do more. Global’s conservation strategy is based on the “water conservation triad”: (1)
13 maximizing use of reclaimed water; (2) using renewable surface water where available; and (3)
14 recharging the aquifer with any available surface or excess reclaimed water. Implementing the
15 triad allows reliance and consumption of non-renewable groundwater supplies to be sharply
16 reduced.

17 **Consolidation.** Arizona has hundreds of small water companies, and many are poorly-
18 capitalized and lack management and technical skills. Through consolidation, well-capitalized
19 companies with experienced management and sophisticated engineering and operations staffs can
20 take the place of these small companies. This results in stable, reliable companies that customers
21 can count on. Consolidated companies also allow economies of scale to be realized. Customers
22 benefit as these lower costs are passed on in the ratemaking process. And consolidation allows
23 companies to access the capital necessary to implement the water conservation triad.

24 **Cooperation.** Effective management of growth occurs when cities, developers, and
25 utilities cooperate. Cities want growth that is sustainable, not reckless. Developers want to make
26 money. Utilities need to be able to manage growth and efficiently utilize available resources.
27 Non-traditional financing methods can align the incentives of developers and utilities to work with

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1 the cities. This allows all three to cooperate to achieve truly sustainable, regionally planned
2 growth.

3 Global Parent's ICFAs, along with its Public Private Partnerships (P3s) with cities, allow
4 Global to implement the 3 C strategy. Traditional financing methods were not designed to allow
5 or support the 3 Cs. Experience shows that utilities that use traditional financing methods do not
6 successfully achieve the 3 Cs. For these reasons, it is in the public interest to allow non-traditional
7 methods, including the ICFAs.

8 These comments will first provide an in-depth explanation of the ICFAs and how they
9 allow the 3 Cs to be realized. Second, although the P3 agreements with the cities do not involve
10 financing, we will briefly explain them as well. Specific answers to the questions posed in the
11 letters of Staff, Commissioner Mundell and Chairman Hatch-Miller will follow.

12 **II. The ICFAs are a flexible means of achieving important objectives not allowed by**
13 **traditional methods.**

14 **A. Description of ICFAs.**

15 As the name implies, ICFAs involve the coordination and financing of utility
16 infrastructure. The ICFAs do not provide for utility services, and Global Utilities are not parties to
17 the ICFAs. Instead, the ICFAs provide for the developer to enter into a main extension agreement
18 with the regulated utility. ICFA, Ex. D and E.¹ The ICFA specifically recognizes that the Global
19 Utilities are separate and distinct companies from Global Parent. ICFA, Recital C.

20 Central to the ICFA is the concept of "carrying costs" or the time value of money. The
21 ICFA provides for payments that are "an approximation of the carrying costs associated with
22 interest and capitalized interest associated with the financing of infrastructure." ICFA, Recital G.
23 Global Parent – not developers – provides the equity for the capital projects of the Global Utilities.
24 ICFA, Recital B. The ICFA payments merely allow Global Parent to plan and deploy
25

26 _____
27 ¹ We will use the ICFA attached to Commissioner Mundell's June 7, 2005 letter as the sample
ICFA, and citations refer to that ICFA.

1 infrastructure to meet the triad of water conservation on a regional scale and cover the time value
2 of the equity it invests – and if Global Parent has overestimated growth, Global Parent, not the
3 regulated utility, not the developer, bears the risk.

4 In enacting our 3C approach, Global Parent undertakes significant entrepreneurial risk.
5 The ICFAs allow Global Parent to reduce its financial exposure as it emplaces hundreds of
6 millions of dollars in infrastructure that is far beyond the norm for any water/wastewater provider,
7 public or private. Global Parent is financing and building the infrastructure necessary to address
8 water scarcity in a fast-growing region – if the growth slows, however, that infrastructure will wait
9 a very long time before becoming ‘used and useful’. Such a risk is inappropriate for a regulated
10 utility, such as the Global Utilities, but well within the capability of the Global Parent’s owners.
11 The ICFAs reduce Global Parent’s risk by providing compensation for the carrying costs – not the
12 principal – of Global Parent’s investment. The ICFAs also shields the Global Utilities from these
13 growth-related risks.

14 Another central concept is openness. The ICFAs are recorded, public documents. The
15 ICFAs are negotiated in a transparent process that where each landowner in an area is offered the
16 same terms. In fact, many ICFAs contain “most favored nation” clauses, which provide that if any
17 other landowner in the area is offered better terms, the protected landowner gets the benefit of
18 those terms. The execution of an ICFA is also a voluntary action on the part of the land owner.
19 Traditional financing methodologies are available at the option of the land owner.

20 The ICFA payments provide for payments tied to various events. Typically, all or a large
21 portion of the ICFA carrying costs are payable at the time of plat approval. For example, in the
22 case of the ICFA attached to Commissioner Mundell’s letter, all the fees are payable upon plat
23 approval. ICFA § 4. In other cases, some of the ICFA fees are payable at certain other defined
24 events, such as when certain permits or certificates are approved.

25 The ICFAs carefully avoid infringing on the Commission’s powers. The ICFAs do not
26 cover rates for utility services, and the Commission, as always, has full authority over the rates
27 charged by the Global Utilities. Likewise, the main extension process is respected. In fact, the

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1 ICFAs require main extension agreements with the Global Utilities, which must be approved under
2 A.A.C. R14-2-406. In addition, the ICFAs carefully respect the Commission’s authority over the
3 CC&N process. Utility service will not be provided to the land until the Commission approves a
4 CC&N, and until a main extension agreement is in place and approved under A.A.C. R14-2-406.
5 If the Commission denies a CC&N for the area, the landowner “may terminate this Agreement
6 without recourse to either party”. ICFA § 7.

7 **B. The ICFAs allow conservation, consolidation, and cooperation.**

8 **1. Conservation.**

9 Water conservation is critically important to the future of our state. For example, a recent
10 report from a committee of the Arizona Department of Water Resources finds that Pinal County
11 has limited groundwater. Recent calculations show that the Pinal Active Management Area
12 (“AMA”) has a renewable groundwater supply of about 82,000 acre feet per year on an average
13 annual basis¹. This represents real “wet water” that will be physically available and can be safely
14 withdrawn over the long term without depleting the aquifer. Yet more than 272,000 acres of land
15 have been issued Irrigation Grandfathered Rights.² At an extinguishment value of 1.5 AF/acre,
16 this represents a potential draw of 408,000 acre feet of “paper water” that could be allocated for
17 withdrawal. Relying on paper water alone will not be sufficient. The water conservation triad can
18 close this substantial gap between paper water and wet water - but only if it is put into effect.

19 Each element of the water conservation triad – reclaimed water, surface water, and water
20 recharged into the aquifer – requires substantial capital. Traditional financing methods are
21 designed to fund only the facilities absolutely necessary to meet the minimum regulatory
22 requirements. It is akin to aiming to get a “D minus” and barely pass. Triad-level facilities are
23 simply not built using traditional methods. Conservation requires doing far more than the
24 minimum. Effective conservation requires – and the Commission should expect – “A plus” work.

25 _____
26 ¹ From the Pinal Active Management Area Groundwater User’s Advisory Committee “Assured
27 Water Supply Modifications Concepts” draft dated December 29, 2005.

² *Id.*

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1 **Reclaimed water** is a good example. ICFA's require developers to use reclaimed water,
2 and they require that reclaimed water facilities be installed. These facilities are not cheap. A basic
3 reclamation system has capital costs of approximately \$5,915 per home.¹ But this investment pays
4 off with a reduction of 30% in potable water consumption, and a 75% reduction in discharges from
5 a wastewater treatment plant – most but not all of the reclaimed water is reused. Installing an
6 advanced reclamation system has capital costs of about \$6,844 per home. An advanced system
7 can expect to reduce potable water usage by 40% and will result in a 100% reduction in
8 wastewater discharges – no reclaimed water will be thrown away, it will all be re-used for some
9 purpose.

10 By covering the carrying costs of these capital investments, the ICFA's enable Global
11 Parent to invest the equity to build reclaimed water facilities. An example is the Belmont master
12 planned community, which is located in western Maricopa County. Belmont will be the largest
13 master planned community with fully integrated water reclamation planning in Arizona. This is
14 only possible because of the ICFA between the developers of Belmont and Global Parent.

15 In addition to preserving groundwater, use of reclaimed water has other benefits. For
16 example, by reducing potable water usage, it also reduces the amount of potable water that must be
17 treated. Why spend money removing arsenic or other “emerging contaminants” from water only to
18 use the expensive treated water to flush toilets or irrigate plants?

19 **Surface water** is another example. Surface water treatment plants are capital intensive and
20 are certainly not cost-effective for smaller individual developments. Because of the ICFA's, Global
21 Parent is currently funding the construction of two regional surface water plants for use by Santa
22 Cruz Water Company.

23 ICFA's also enable Global Parent to pay for other items necessary to surface water use, such
24 as CAP fees prior to usage, water leases or options for leases, and protecting the Maricopa
25 Stanfield Irrigation and Drainage District's canal systems, so that surface water can be delivered to
26

27 ¹ The price per home is computed on a “equivalent dwelling unit” basis.

1 treatment plants. Traditional funding mechanisms, such as main extension agreements and hook-
2 up fees are limited to specific facilities, and cannot be used for such items. In addition, the
3 Commission will typically not allow a utility to recover such items unless they are “used and
4 useful”. But investment in such items must often be made well before they will become used and
5 useful. The ICFAs provide an answer – they bridge between upfront regional construction costs
6 and those facilities becoming “used and useful”.

7 **Recharged water.** The demand for reclaimed water varies by season because in the winter
8 there is less need for irrigation. The availability of surface water can also vary – for example, due
9 to canal repair, seasonal variations in irrigation usage, or unexpected rainfall. Thus, there will be
10 times when excess reclaimed water and surface water are available. This excess water can be
11 recharged into local aquifers, so that it can be used again later, when supplies are tighter.

12 As with the other elements of the triad, there are capital costs for building recharge
13 facilities. By covering the carrying costs of this capital, the ICFAs allow Global Parent to invest in
14 these facilities. Moreover, recharge should be local. “Replenishment” by the CAGR D typically
15 results in recharging water far away from a utility’s wells – creating paper water not wet water.
16 Few utilities take the extra step and build their own recharge facilities to recharge their local
17 supplies.

18 As the saying goes, the proof is in the pudding. Utilities using traditional financing do not
19 utilize the water conservation triad. At most, they may scrape together funds to partly implement
20 one element of the triad. In contrast, Global has been – and will continue to be – at the very
21 forefront of water conservation in Arizona. There is no utility in this state that can match Global’s
22 record, and this record is only possible due to the ICFAs.

23 2. *Consolidation.*

24 Another important use of ICFAs is to help fund consolidation. Consolidation allows the
25 utility to gain (1) economies of scale; (2) better access to debt and equity capital; and (3) more
26 sophisticated, capable management. Unfortunately, the economics of acquisitions often do not
27 work for small companies. They often have little or no rate base, so their rates will be low. Yet

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1 the owners are reluctant to sell for a low price. When the buyer pays more than book value, the
2 Commission almost never allows the resulting "acquisition adjustment" into rate base. The buyer
3 thus does not earn a return on this part of their investment. The ICFAs change the situation. For
4 example, developers in the service area of a small, marginally viable utility often fear the results of
5 a failed company on their land values. They are therefore motivated to find a better capitalized,
6 more capable provider. Part of the "acquisition adjustment" can be built into the ICFA costs. The
7 utility, the developer, and most importantly, the customer all benefit. Consolidation is a goal
8 favored by the Commission. ICFAs allow developers to pay to achieve this goal.

9 **3. Cooperation.**

10 The ICFAs allow Global to promote cooperation with cities and others. For example, the
11 Cities of Maricopa and Casa Grande are very concerned about future water supplies. The ICFAs
12 allow Global to carry out the water conservation triad. This allowed Global to address the cities'
13 concerns. Out of this cooperative relationship, the P3 agreements were negotiated, publicly
14 debated at Council meetings and approved by open vote. These relationships provide for yet more
15 cooperation and joint planning.

16 Another example is Global's relationship with our neighbors in the Ak-Chin Indian
17 Community ("Community"). The Community expressed cultural and environmental concerns
18 regarding the possibility of reclaimed water being discharged into certain washes. Although
19 Global is at the forefront of reclamation and re-use, there were still occasions when reclaimed
20 water was not being reused, for example during particularly rainy periods. The Ak-Chin grew
21 concerned over the amount of development planned upstream of their washes. These washes have
22 very significant cultural meaning to the Community. Because of the ICFAs, and the significant
23 financial resources they allow us to deploy, Global was able to address the Ak-Chin's concerns
24 and devise a sophisticated recharge plan that will augment our reuse plans and ensure that no
25 reclaimed water will be discharged into any wash leading into the Ak-Chin Community. This led
26 to an unprecedented letter of understanding between Global Parent and the Ak-Chin Community
27 and a very positive and close working relationship. A copy of this letter is attached as Exhibit A.

1 The ICFAs also allow cooperation with developers. For example, Global Parent has
2 worked with developers to buy troubled systems using ICFAs. In addition, the ICFAs do not
3 require developers to borrow money to make huge upfront payments to the utility, as often
4 happens with main extensions. By restructuring the timing of payments, Global Parent is able to
5 make the ICFAs attractive to developers, who agree to the other aspects of the ICFA – such as
6 promotion of reclaimed water and surrender of groundwater wells – as part of the package.

7 **C. ICFAs are not main extensions.**

8 ICFAs are very different from main extension agreements. The ability to do regional
9 planning, the timing of when facilities are constructed and when developers pay, who actually does
10 the construction, and the functions that can be financed are all sharply different. In addition the
11 parties are different, because utilities are parties to main extension agreements but not ICFAs.

12 A key difference is in regional planning. Main extensions are done on a parcel by parcel
13 basis. A developer pays for the facilities need to serve their development only. A.A.C. R14-2-
14 406(B)(1). This typically results in things like small, highly inefficient “package” treatment
15 plants. In contrast, under the ICFA, Global plans and constructs regional facilities to gain
16 economies of scale. For example, Global puts in large 48 inch collection mains. Under a main
17 extension approach, multiple smaller lines would eventually be constructed instead, often running
18 parallel to each other.

19 The timing of construction is also different. Main extensions must be processed in the
20 “order received.” A.A.C. R14-2-406(J). If a utility gets main extension requests for opposite ends
21 of its service area at the same time, it must build them both, rather than waiting for neighboring
22 development to fill in. This reinforces the tendency to build small, inefficient facilities because
23 the utility can’t afford to “upsized” them for future growth. Under the ICFA, Global Parent is able
24 to coordinate the timing of construction. This reinforces Global Parent’s ability to plan and build
25 large regional facilities.

26 Moreover, under a main extension approach, the construction is usually done by the
27 developer, who then turns the facilities over to the utility. In contrast, under the ICFA, “off-site”

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1 facilities are utility built. This results in developers building homes, and utilities building utility
2 plant.

3 Most fundamentally, ICFAs and main extension agreements pay for different things. Main
4 extensions can only pay for facilities. A.A.C. R14-2-406(B)(1). ICFAs only pay the carrying costs
5 associated with the provision of facilities. And they can be used for many things that are not
6 facilities at all. This includes forming new utilities, consolidating existing utilities, paying for
7 CAP reservation fees, and paying for the protection of canal systems.

8 **D. ICFAs are not like hook-up fees.**

9 There are also many differences between ICFAs and hook-up fees. For example, hook-up
10 fees are mandatory, while ICFAs are voluntary. In addition, hook-up fees result in high levels of
11 contributions in aid of construction (“CIAC”), while ICFAs result in equity.

12 Hook-up fees are allowed only for specific future infrastructure.¹ In contrast, the ICFA
13 allows the utility to control the timing of construction. More importantly, hook-up fees are limited
14 to infrastructure.² In contrast, as noted above, ICFAs can be used for many important uses other
15 than physical infrastructure, such as the consolidation of utilities.

16 **III. The P3s are in the public interest.**

17 The P3s are not financing agreements. Instead, they merely provide for cooperation
18 between Global and the cities. The P3s are public documents adopted after open and full
19 deliberation by the Cities of Maricopa and Casa Grande. The P3s with Maricopa and Casa
20 Grande are attached as Exhibits B and C, respectively. The P3s serve many beneficial purposes.
21 They help the cities cope with growth. Indeed, one of the core purposes of the P3s is to help the
22 cities manage growth in accordance with Arizona’s Growing Smarter and Growing Smarter Plus
23 laws. Casa Grande P3, page 1. For example, Global must prepare an annual “Plan for Growth”
24 for the city’s planning area. *Id.* at ¶ 10. Global will also share its Geographical Information

25
26 ¹ See Staff Memorandum filed June 8, 2006 in Docket No. W-01303A-06-0284.

27 ² *Id.*

1 System ("GIS") with the city. *Id.* ¶ 13. Global is also obligated to support the City's annexation
2 efforts. *Id.* ¶ 14. Global will work with the City to manage and coordinate development. *Id.* In
3 addition, the P3s strongly promote the use of reclaimed water and water conservation measures.
4 *Id.* ¶¶ 8, 12.

5 By these measures, the cities and Global establish a close working relationship, so that they
6 can both better serve the public. To that end, the P3s include provisions for extensive
7 communication and cooperation between the cities and Global. *Id.* at ¶¶ 1-3, 6. Global is strongly
8 committed to a close and cooperative relationship with the cities. Global believes that a
9 cooperative, not hostile, approach is in the public interest.

10 Moreover, the P3s in no way grant a right to serve any area. The P3s do not create an
11 exclusive relationship, and other utilities can enter such agreements if they choose.¹ The P3s
12 carefully respect the Commission's authority to designate service areas through the CC&N
13 process. Thus, they only provide for the cities to participate in the CC&N process. *Id.* at ¶ 17(a).

14 The P3s also carefully respect the Commission's ratemaking powers. The P3 with Casa
15 Grande provides for Global Parent to pay a fee of \$100 to the city for each residential home
16 connecting to the regulated subsidiaries. *Id.* at ¶ 10. In addition, Global Parent agreed to pay Casa
17 Grande a fee of 3% (in some cases, 2%) of gross revenues of the regulated subsidiaries within the
18 relevant area. *Id.* at ¶ 4. The P3 does contemplate these fees might be passed on to customers.
19 But the P3 clearly states that this fee cannot be included in the customer's bill unless it is
20 specifically approved by the Commission. *Id.* The Global Utilities have not requested such
21 approval. Accordingly, there is no charge on customer bills. Again, the P3 specifically requires
22 Commission approval before any customer is charged. Global Parent has elected, for the time
23 being, to simply pay the fees itself at the parent company level rather than seek approval for
24

25
26
27 ¹ The P3s have no provisions for exclusivity. Further, the fact that the P3s are non-exclusive was
made clear at the public hearings on the P3s conducted by the cities of Maricopa and Casa Grande.

1 regulated utility recovery. Under the P3, the fees are simply an operating expense of Global
2 Parent. *Id.*

3 The P3s provide for close cooperation with the cities, while still preserving the
4 Commission's authority in all respects. The P3s are thus in the public interest.

5 **IV. Response to letters in the docket.**

6 **A. Response to Staff's June 2, 2006 Letter.**

7 **Question 1.A:** A developer purchases a non-regulated parent company's non-voting stock.
8 Each of the non-voting shares has a par value of \$1.00, is not eligible for dividends, is partially
9 refundable and can be repurchased (subject to certain conditions) by the non-regulated parent for
10 one cent (\$0.01).... The parent company subsequently contributes the funds to an ACC regulated
11 subsidiary water utility as additional paid-in capital.

12 **Response:** Global has no opinion regarding this scenario.

13
14 **Question 1.B:** A developer purchases a regulated utility's non-voting stock and that utility
15 invests those funds in plant. The utility records equity for the proceeds. Neither refundable
16 advances in aid of construction nor contributions in aid of construction are recorded.

17 **Response:** The sale of preferred or common stock to a developer can be a legitimate
18 source of equity, as long as the transaction is voluntary and not constructed as a "sham" and is not
19 a requirement for getting service within an existing service area. However, Global notes that it
20 does not use this model. Although some of Global Parent's owners are developers, as a matter of
21 policy, Global Parent does not operate in areas being developed by its owners, to avoid any
22 conflicts of interest or appearance of favoritism.

23
24 **Question 1C:** A developer or a Municipal Government pays a fee for services provided by
25 a non-regulated parent company for services typically covered by "Off-site Hook-up Fees"
26 collected by regulated water and wastewater utilities. Then the parent company invests the
27 proceeds in the regulated utility which is recorded as equity by the utility.

1 **Response:** If this question is intended to refer to the ICFAs, Global notes that they are not
2 like hook-up fees for the reasons stated above. Please see Section II above for a description of
3 how the ICFAs actually operate.
4

5 **Question 2:** What is the maximum percentage of refundable "Advances in Aid of
6 Construction" ("AIAC") appropriate as a percentage of total capital for a private or investor owned
7 water utility?

8 **Response:** The amount of AIAC and CIAC that is appropriate depends on the
9 circumstances. Global generally agrees with Staff that AIAC and CIAC should ideally not exceed
10 30% of total capital.¹ However, this rule of thumb should not be applied inflexibly. For example,
11 if the utility has a high level of equity, it may be able to absorb more AIAC. In addition, the
12 capital structure over time should be considered. For example, it might be appropriate for a utility
13 to start with a higher level of AIAC if it has well-capitalized parent and plans on using equity to
14 fund future capital needs. In addition, the rate of refunds of AIAC should be considered. On one
15 hand, refunds build up rate base because they reduce AIAC (which is a negative element of rate
16 base). On the other hand, refunds require cash flow.
17

18 **Question 3:** What is the maximum percentage of non-refundable "Contributions in Aid of
19 Construction" ("CIAC") appropriate as a percent of total capital for a private or investor owned
20 water utility?

21 **Response:** See response to question 2.
22

23 **Question 4:** What is the most appropriate and most economical capital structure for a
24 "new" water or wastewater utility?
25
26

27 ¹ See Staff Report filed May 26, 2006 in Docket No. SW-20422A-05-0659 at Ex. 2.

1 **Response:** There is no one best capital structure for a new utility. The appropriate capital
2 structure will be affected by numerous factors, including estimated growth rates, estimated future
3 capital needs, estimated cash flow, and whether the initial rates cover the utility's costs, including
4 capital costs. In general, a capital structure should avoid excessive amounts of AIAC, CIAC, and
5 debt. Excessive amounts of those elements would result in a financially weak utility. As long as
6 this is avoided, though, the utility's capital structure should be a matter of discretion left to the
7 management's financial judgment.

8 **B. Response to Commissioner Mundell's June 7, 2006 letter.**

9 • **Invitation for presentation.**

10 Global looks forward to giving the requested presentation, and is already developing a
11 thorough briefing for the Commissioners.

12 **Question 1 – P3 Agreements.**

13 The P3 Agreements are described in Section III above, and copies of the P3s are attached
14 for your reference.

15 • **Are these [P3] arrangements intended to be municipal operations not
16 subjected to the Commission's jurisdiction?**

17 Definitely not. The P3s have no similarity to "management agreements" like the
18 agreement for the former Skyline District. Service is provided by the Global Utilities through their
19 own resources. The Global Utilities remain fully subject to the Commission's jurisdiction in all
20 respects. Global Parent's business model has always been to own regulated utilities. As described
21 in Section III above, the P3s carefully respect the Commission's authority, including its rate and
22 CC&N powers.

23 **Question 2 – ICFAs.**

24 • **GWR's perspective on the role of the Arizona Corporation Commission
25 regarding these agreements.**

26 The Commission is not directly involved in the ICFAs because they operate at a holding
27 company level and do not involve the provision of utility services. However, the Commission

1 retains full authority over the CC&N process. If the CC&N is not granted, the ICFA has little
2 value, and the landowner has the option of cancelling it. This means that Global Parent is taking
3 an entrepreneurial risk – a risk not appropriate for any regulated utility, such as the Global
4 Utilities. If growth fails to develop as planned, it is Global Parent that will have sunk large
5 amounts of money into unused infrastructure. In addition, the Commission, through its Staff, will
6 still review the related main extension agreements in accordance with A.A.C. R14-2-406. The
7 Commission also retains full authority over the Global Utilities, including their rates and service
8 quality.

9 • **The nature of the “per dwelling unit” fees charged by GWR.**

10 These fees are based on the carrying costs of the capital necessary to serve the
11 development. In addition, other costs may be factored in, such as the cost of acquiring an existing
12 utility, or the costs of acquiring access to surface water. The fees are negotiated. The developers
13 who sign the ICFAs are typically very sophisticated. The same fees apply to an entire area, so that
14 there is no discrimination. This means that Global Parent is often negotiating with multiple
15 developers at once.

16 • **From afar, they resemble “hook-up” fees? Are they? If so, please explain the
17 legal basis for these fees when GWR is not a Public Service Corporation (PSC).**

18 The ICFA fees are not hook up fees. A key difference is that hook-up fees can only be
19 used for a single purpose - to fund specific future infrastructure, while ICFA fees can be used for
20 many purposes, such as funding consolidation and conservation efforts. In addition, hook-up fees
21 are mandatory, while ICFA fees are entirely voluntary. Inside the existing CC&N area of a Global
22 Utility, the landowner always has the option of signing a traditional main extension agreement.
23 Outside the current CC&N area, the landowner can always request service from another utility, or
24 even form its own utility if allowed by the Commission. Additional differences between ICFAs
25 and hook up fees are discussed in Section II.D above.
26
27

1 • **If these fees are not for utility infrastructure, than what are the developers**
2 **receiving for these fees.**

3 The developers are entering into a financing agreement. They only pay carrying costs on
4 the equity deployed by Global Parent. The actual cost of facilities is much greater, especially since
5 Global builds the entire triad of water conservation – facilities for reclaimed water, surface water,
6 and recharge. The timing of the payments is also more favorable than traditional methods. Again,
7 no developer is ever forced to sign an ICFA – it is entirely voluntary.

8 • **Why do customers need a middleman to “coordinate” or even supply services**
9 **that are by law required to be provided by the referenced PSCs... The CC&Ns held by these**
10 **companies seem to be legally sufficient to ensure service. Please explain.**

11 The ICFAs do NOT provide for utility services. A developer does not receive a drop of
12 water under an ICFA. If the developer is outside a CC&N area, they are free to seek service from
13 any other provider, or to form their own provider, if the Commission allows. If the developer is
14 within a current CC&N area, the developer is always free to enter in to a traditional main
15 extension agreement. Either way, the ICFA is entirely voluntary. Developers – including highly
16 sophisticated, nationally prominent developers -- choose to sign these agreements because they
17 find value in the financing and coordination services provided, as compared with traditional
18 models.

19 Often ICFAs involve areas outside of current CC&Ns, or involve land trapped within the
20 service area of utility whose capabilities are subject to question. The Global Utilities have no
21 current obligation to serve such areas, but Global Parent is always happy to explore such
22 possibilities.

23 Global wholeheartedly agrees that within an existing CC&N area, the utility has an
24 obligation to serve. Within the CC&Ns of the Global Utilities, a developer can always sign a
25 traditional main extension agreement.

26 • **“Impact of poorly run operations and lack of available capital”**
27

1 Global agrees that these are very serious problems. The ICFA's are designed, in part, to
2 provide a mechanism to solve these problems, as well as enabling the full triad of water
3 conservation measures to be implemented.

4 **C. Response to Chairman Hatch-Miller's letter dated June 12, 2006.**

5 Global agrees that having "well-capitalized private water/wastewater utilities, with
6 experienced and knowledgeable operational and managerial staff" is vital to our state.

7 **V. Conclusion.**

8 Global appreciates this opportunity to respond to questions and concerns about the ICFA's
9 and the P3s. The ICFA's and the P3s were designed with openness in mind - the ICFA's are
10 publicly recorded documents and the P3s were adopted in open public meetings of the City
11 Councils - and we welcome the spotlight on them. Global looks forward to giving the
12 presentation requested by Commissioner Mundell and Chairman Hatch-Miller. Global is also
13 happy to answer any further questions that Staff or the Commissioners may have about these
14 topics.

15 In the end, the ICFA's results in a direct reduction groundwater consumption in our state.
16 Average per dwelling unit potable water consumption for non-integrated, traditionally financed,
17 Arizona utility service providers is in the order of 13,500 gallons per month. By impressing the
18 3C's into the planning program, Santa Cruz Water Company's monthly average demand in the
19 first phase of development in the City of Maricopa is 8,200 gallons per month per unit.

20 Going further, by using the triad of conservation and enforcing re-use and reclamation as
21 policy, subsequent phases in the City of Maricopa have achieved even greater success. There has
22 been a 90% reduction in irrigation meters supplied by potable water. As a result, the actual
23 potable demand in these reclamation-minded areas is 5,700 gallons per month dwelling unit - a
24 30% reduction over Santa Cruz's initial service areas, and a staggering 57% reduction in potable
25 water consumption over traditionally structured Arizona utility services. This is the power of an
26 ICFA-funded conservation strategy - direct, measurable and immediate resource conservation.

27

1 RESPECTFULLY SUBMITTED this 23rd day of June 2006.

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3
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