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AZ CORP COMMISSION  
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Attorneys for Northern Sunrise Water Company  
and Southern Sunrise Water Company

**BEFORE THE ARIZONA CORPORATION COMMISSION**

IN THE MATTER OF THE APPLICATION OF  
NORTHERN SUNRISE WATER COMPANY  
FOR A CERTIFICATE OF CONVENIENCE  
AND NECESSITY TO PROVIDE WATER  
UTILITY SERVICE IN COCHISE COUNTY,  
ARIZONA.

DOCKET NO. W-20453A-06-0247

IN THE MATTER OF THE APPLICATION OF  
SOUTHERN SUNRISE WATER COMPANY  
FOR A CERTIFICATE OF CONVENIENCE  
AND NECESSITY TO PROVIDE WATER  
UTILITY SERVICE IN COCHISE COUNTY,  
ARIZONA.

DOCKET NO. W-20454A-06-0248

IN THE MATTER OF THE JOINT  
APPLICATION OF NORTHERN SUNRISE  
WATER COMPANY AND SOUTHERN  
SUNRISE WATER COMPANY FOR THE  
APPROVAL OF SALE AND TRANSFER OF  
WATER UTILITY ASSETS, AND  
CANCELLATION OF CERTIFICATES OF  
CONVENIENCE AND NECESSITY, FOR  
MIRACLE VALLEY WATER COMPANY,  
COCHISE WATER COMPANY, HORSESHOE  
RANCH WATER COMPANY, CRYSTAL  
WATER COMPANY, MUSTANG WATER  
COMPANY, CORONADO ESTATES WATER  
COMPANY, AND SIERRA SUNSET WATER  
COMPANY, LOCATED IN COCHISE  
COUNTY, ARIZONA.

DOCKET NOS. W-20453A-06-0251  
W-20454A-06-0251  
W-01646A-06-0251  
W-01868A-06-0251  
W-02235A-06-0251  
W-02316A-06-0251  
W-02230A-06-0251  
W-01629A-06-0251  
W-02240A-06-0251

**EXCEPTIONS TO RECOMMENDED OPINION AND ORDER**

Pursuant to A.A.C. R14-3-110(B), Northern Sunrise Water Company ("Northern")  
and Southern Sunrise Water Company ("Southern") (collectively herein, "Applicants"),

1 submit these Exceptions to the Recommended Opinion and Order (“ROO”) dated June 21,  
2 2006.

3 **I. OVERVIEW AND SUMMARY OF APPLICANTS’ EXCEPTIONS.**

4 Applicants have submitted three applications related to their proposed acquisition  
5 of the seven water utility systems known as the McLain Systems. The Arizona  
6 Corporation Commission (“Commission”) is well aware of the troubled history of these  
7 water systems and has repeatedly expressed its desire to have a qualified water utility  
8 provider take over service to the beleaguered McLain ratepayers. Given the shortness of  
9 time available to Applicants and the Commission, a reiteration herein of the background,  
10 procedural history and critical facts underlying the three applications (as well as these  
11 Exceptions) is not possible. For now, it will have to suffice to remind this Commission  
12 that, despite the Herculean efforts of the Utilities Division Staff (“Staff”) and  
13 Administrative Law Judge (“ALJ”) Rodda, acquisition of the McLain Systems continues  
14 to pose substantial risk to the Applicants. The modifications to the ROO requested in  
15 these Exceptions are intended to reduce that risk to a level acceptable to Applicants. For  
16 the convenience of the Commission, Applicants’ Exceptions are briefly summarized  
17 immediately below, and then discussed in greater detail in the remainder of this filing.

18 **A. Babocomari Conditions.**

19 The ROO’s requirement that inclusion of the Babocomari  
20 Development in the Northern Certificate of Convenience and Necessity  
21 (“Certificate of Convenience and Necessity”) be conditioned on the filing of  
22 a Letter of Water Adequacy is contrary to the public interest as presented in  
23 the unique circumstances presently before the Commission. The record  
24 reflects that there is adequate water available for Northern to serve this new  
25 development area. The imposition of additional requirements that would  
26 not otherwise exist, but for the Commission’s order, is not only unfair to the  
property owners and Applicants, but would place in jeopardy the  
landowners’ gift of an ideal site for construction of storage and booster  
facilities needed to bring the McLain Systems into compliance.  
Additionally, the requirement places the potential growth in the systems at

1 risk, a potential that is the primary incentive for Applicants' willingness to  
2 take over the McLain Systems. Those risks outweigh any stated interest in a  
3 formalized finding of water adequacy where one is not otherwise required.

4 **B. Lifting of Existing Moratoria.**

5 Applicants understand the need for the Commission to continue the  
6 moratoria on new connections currently in effect for the McLain Systems  
7 until such time as necessary system improvements are completed. At that  
8 time, however, Applicants continue to advocate for a process that is timely.  
9 The ROO's allowance of more time for Staff to respond to notification that  
10 improvements are complete is objectionable.

11 **C. Recovery of Transaction Costs.**

12 Applicants have and will continue to incur significant costs  
13 associated with the acquisition of the McLain Systems. Applicants require a  
14 clear and unambiguous finding by this Commission in these dockets that up  
15 to \$300,000 of such expenses are reasonable and prudent and recoverable  
16 from ratepayers, subject only to verification in future proceedings of actual  
17 cost being incurred in connection with the transaction. In addition,  
18 Applicants require Commission assurance that the additional costs  
19 associated with compliance with the Decision in these dockets will be  
20 recoverable through rates.

21 **D. Timing of Tariff Filings.**

22 The ROO's requirement that Applicants file a Backflow Prevention  
23 Tariff and Curtailment Plan within 45 days of the Decision should be  
24 modified to require such filings within 45 days of the close of the sale  
25 transaction to avoid Applicants having to make such filings before they  
26 actually acquire the assets of the McLain Systems.

**E. ASUA Transition.**

The ROO should be modified to make it absolutely clear that  
Applicants bear no responsibility for transitioning the Commission's Interim  
Operator, ASUA, out of its role.

1     **II.     APPLICANTS' EXCEPTIONS TO THE RECOMMENDED OPINION AND**  
2     **ORDER DATED JUNE 21, 2006 AND REQUESTS FOR CLARIFICATION.**

3     **A.     Conditioning Inclusion Of The Babocomari Development On A Letter**  
4     **Of Water Adequacy Is Unfair To Property Owners And Would**  
5     **Frustrate The Public Interest As Well As Applicants' Incentive For**  
6     **Taking Over The McLain Systems.**

6             In its Application, Northern sought to include an area known as the Babocomari  
7     Development, a currently undeveloped area not included in any of the McLain Systems'  
8     CC&Ns. Northern's request was based on a request for service from the landowners and  
9     on the willingness of those landowners to contribute a parcel of land upon which storage  
10    tanks and booster facilities necessary to improve the McLain Systems can be sited. ROO  
11    at 6. Northern's request was also consistent with its primary motivation for agreeing to  
12    acquire the McLain Systems—that being the potential for growth in these systems as  
13    represented primarily by the Babocomari Development.

14            Regarding inclusion of the Babocomari Development in Northern's CC&N, the  
15    ROO concludes that "it is not in the public interest nor good policy to grant a CC&N  
16    where there is no demonstration of adequate water supply." ROO at 8. While the  
17    Applicants generally agree with such an assertion, the circumstances presented in these  
18    dockets are unique and require extraordinary relief. The Applicants have already  
19    demonstrated that there is an adequate water supply to serve the development. The  
20    developers of the Babocomari area have commissioned a hydrology study for the project  
21    by Errol L. Montgomery & Associates. ROO at 6. That report, which appears to have  
22    been ignored by Staff, concluded that there was adequate water available to meet the  
23    needs of the development.<sup>1</sup> The requirement for any greater showing is unnecessary and  
24    impractical.

25            <sup>1</sup> During the hearing, Staff's witness testified that he had not reviewed and was unaware of the hydrology  
26    report for the Babocomari Development included in Northern's CC&N application. Hearing Transcript  
  ("TR") at 255.

1 The owners of the Babocomari Development are not legally obligated to obtain the  
2 Letter of Water Adequacy the ROO would require. TR at 258. Accordingly, the  
3 Commission would be imposing water adequacy and land-use planning requirements on  
4 landowners that may be in excess of those required by the Arizona Department of Water  
5 Resources, the agency charged with the duty to regulate use of the State's water resources,  
6 and Cochise County, the local land-use planning agency. Applicants respectfully suggest  
7 that the Commission should avoid such excessive regulation, especially in this case.

8 As an element of providing service to the Babocomari development, the  
9 landowners have agreed to provide Applicants with a well situated property for the  
10 placement of storage and booster facilities that will substantially improve the adequacy  
11 and reliability of water service to existing customers of the McLain Systems. TR at 48-  
12 51. This land-gift would save Applicants the time and cost to purchase or condemn that  
13 site, or an inferior alternative site. Any additional costs necessitated by such acquisition  
14 will ultimately burden the ratepayers, who are already shouldering the cost of the previous  
15 owners' acts and omissions. *Id. See also* ROO at 7.

16 If the ROO's condition of a Letter of Water Adequacy is adopted by the  
17 Commission (which condition is beyond the requirements to which the Babocomari  
18 Development is otherwise subject), it is reasonable to expect that the landowners will seek  
19 water service in some other manner and not provide Applicants with the land parcel for  
20 placement of critical utility improvements. TR at 51. *Id.* In that event, not only will  
21 Applicants lose the site for locating facilities, but they will be deprived of one of the  
22 primary reasons they are willing to take over the McLain Systems—the potential for  
23 future growth in the region. Accordingly, conditioning the inclusion of the Babocomari  
24 Development in the Northern CC&N on a Letter of Water Adequacy as proposed would  
25 clearly frustrate the public interest.

26

1           **B. The ROO's Recommended Procedures For Lifting Existing Moratoria**  
2           **On New Connections Are Unnecessarily Burdensome.**

3           Given the dreadful condition of the McLain Systems, Applicants have never  
4 objected to continuation of the Commission-imposed moratoria on new connections  
5 following acquisition. However, Applicants do object to the ROO's proposed process for  
6 the lifting of individual moratorium because such process would allow Staff to delay the  
7 lifting of the moratorium by seeking an extension of the time for responding to  
8 Applicants' notice beyond the allotted 20 days. ROO at 26.

9           ADEQ is the appropriate entity to assist Applicants in making the technical  
10 determinations necessary to improve the McLain Systems and ADEQ will be responsible  
11 for issuing the requisite approvals for new construction. If all matters necessary to bring  
12 the systems into compliance are not completed to ADEQ's satisfaction, including well  
13 capacity, pumping capacity, storage capacity, pipe pressure, then the systems will not be  
14 in compliance and Applicants will be subject to violations and enforcement actions by  
15 ADEQ. Accordingly, Staff can and should rely on ADEQ's jurisdiction in this area and  
16 will be able to promptly confirm that the notice supports lifting of the moratorium without  
17 the need for extensions of time that prejudice Applicants.

18           **C. The Commission Should Make It Clear That Applicants' Transaction**  
19           **Costs Will Not Be Subject To A Prudency-Type Review In Future Rate**  
20           **Cases.**

21           Applicants were also "puzzled" by Staff's recommendations concerning recovery  
22 of transaction costs and, at one time, shared the ROO's conclusion that the dispute  
23 between them and Staff over future review of transaction costs might simply "be an issue  
24 of semantics." ROO at 12. This was the case until Staff's witness testified that Staff's  
25 recommendation actually was to "defer a prudency analysis of the transaction costs for the  
26 future rate case." TR at 273.

1 To make the Applicants' position regarding recovery of all transaction costs clear:

2 1. Applicants require the Commission's unambiguous declaration that the  
3 transaction costs actually being incurred by Applicants are appropriate to further the  
4 public interest and are reasonable and prudent, to a maximum amount of \$300,000, and  
5 that recovery of such costs is subject only to a future verification of the actual amount  
6 spent or incurred to further the transaction.

7 2. All reasonable costs incurred in compliance with the Decision in this docket,  
8 including, without limitation, the costs of filing future applications to extend the  
9 respective CC&Ns for Northern and Southern, proceedings related to lifting of the  
10 moratoria and other compliance filings. As reflected herein, and in the ROO, Applicants  
11 have objected to the use of continuing Commission proceedings to further effectuate the  
12 transfer of operations to Applicants. If the Commission nevertheless elects to impose  
13 numerous future compliance requirements on Applicants, it must also ensure that the  
14 reasonable costs of such compliance are fully recoverable through rates charged to  
15 Applicants' future customers. Furthermore, it should be clear that such assurance of  
16 recovery is separate and apart from the \$300,000 cap on transaction costs Applicants have  
17 agreed to accept.

18 **D. The Deadline For The Filing Of Backflow And Curtailment Tariffs**  
19 **Should Be Triggered By The Close Of The Sale Transaction.**

20 Applicants do not object to being required to file a Backflow Prevention Tariff or  
21 Curtailment Plan in the forms found on the Commission's website. ROO at 21, 34. However,  
22 the requirement that these filings be made within 45 days of the Decision places the Applicants  
23 in the possible position of having to file the tariff and plan *before* they actually own the assets.  
24 The date of the closing of the actual acquisition is, to a great extent, outside Applicants'  
25 control. Accordingly, the ROO should be modified to require the filing of a Backflow  
26 Prevention Tariff and Curtailment Plan within 45 days of the closing of the sale transaction.

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**E. The ROO Should Be Clarified To Provide Applicants Unambiguous Assurance That Removal Of ASUA As Interim Operator And All Related Matters Are The Responsibility Of The Commission And Its Staff.**

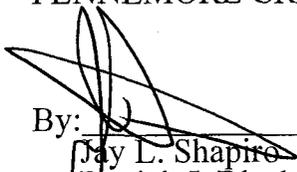
Applicants request confirmation that none of the matters addressed in the ROO respecting ASUA, including elimination of the SIS recently approved in Decision No. 68667, will be their responsibility. ROO at 21-23.

**III. CONCLUSION.**

The Commission, its Staff and the Hearing Division, along with the Applicants and other interested stakeholders, have worked very hard to reach the point of bringing an order before the Commission that will further the public interest by providing the authority necessary before Applicants can take over service to customers of the McLain Systems. The ROO brings the interested stakeholders much closer to achieving that goal. However, the modifications to the ROO outlined by Applicants in these exceptions are necessary if the goal of Applicants acquiring the McLain Systems and taking over service to those customers is to be accomplished. Accordingly, Applicants respectfully request that the Commission consider these Exceptions and make the necessary modifications to the ROO in its final order in these consolidated dockets.

DATED this 26<sup>th</sup> day of June, 2006.

FENNEMORE CRAIG, P.C.

By:   
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1 ORIGINAL and 33 copies of the foregoing  
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2 Docket Control  
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5 COPY hand-delivered this  
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