

ORIGINAL



0000068495

RECEIVED

32R

1 FENNEMORE CRAIG, P.C.
 2 Jay L. Shapiro (No. 014650)
 3 Patrick J. Black (No. 017141)
 4 3003 North Central Avenue, Suite 2600
 5 Phoenix, Arizona 85012
 6 Telephone (602)916-5000
 7 Attorneys for Pine Water Company

2007 DEC -5 P 4:49

AZ CORP COMMISSION
DOCKET CONTROL

BEFORE THE ARIZONA CORPORATION COMMISSION

8 IN THE MATTER OF THE APPLICATION
 9 OF PINE WATER COMPANY FOR
 10 APPROVAL TO (1) ENCUMBER A PART
 11 OF ITS PLANT AND SYSTEM
 12 PURSUANT TO A.R.S. § 40-285(A); AND
 (2) ISSUE EVIDENCE OF
 INDEBTEDNESS PURSUANT TO A.R.S.
 § 40-302(A).

DOCKET NO: W-03512A-07-0362

NOTICE OF FILING

13 Pine Water Company, Inc. hereby submits the Notice of Filing in the above-
 14 referenced matter. Attached hereto as Exhibit A is the Rebuttal Testimony of
 15 Robert T. Hardcastle.

16 DATED this 5th day of December, 2007.

FENNEMORE CRAIG, P.C.

By 

Jay L. Shapiro
 Patrick J. Black
 3003 North Central Avenue
 Suite 2600
 Phoenix, Arizona 85012
 Attorneys for Pine Water Company

Arizona Corporation Commission
DOCKETED

DEC 5 2007

DOCKETED BY 

1 **ORIGINAL** and thirteen (13) copies of the
2 foregoing filed this 5th day of December, 2007:

3 Docket Control
4 Arizona Corporation Commission
5 1200 W. Washington St.
6 Phoenix, AZ 85007

7 **COPY** of the foregoing hand-delivered
8 this 5th day of December, 2007

9 Mr. Dwight D. Nodes
10 Assistant Chief Administrative Law Judge
11 Arizona Corporation Commission
12 1200 W. Washington Street
13 Phoenix, AZ 85007

14 Mr. Kevin Torrey, Esq.
15 Legal Division
16 Arizona Corporation Commission
17 1200 West Washington Street
18 Phoenix, Arizona 85007

19 **COPY** of the foregoing **emailed**
20 this 5th day of November, 2007 to:

21 jgliege@earthlink.net; jgliege@gliege.com
22 John G. Gliege
23 Gliege Law Offices, PLLC
24 P.O. Box 1388
25 Flagstaff, AZ 86002-1388

26 By: *Marisa Sam Joe*
2006675.1

Exhibit A

1 FENNEMORE CRAIG, P.C.
2 Jay L. Shapiro (No. 014650)
3 Patrick J. Black (No. 017141)
4 3003 North Central Avenue, Suite 2600
5 Phoenix, Arizona 85012
6 Telephone (602)916-5000
7 Attorneys for Pine Water Company

8 **BEFORE THE ARIZONA CORPORATION COMMISSION**

9 IN THE MATTER OF THE APPLICATION
10 OF PINE WATER COMPANY FOR
11 APPROVAL TO (1) ENCUMBER A PART
12 OF ITS PLANT AND SYSTEM PURSUANT
13 TO A.R.S. § 40-285(A); AND (2) ISSUE
14 EVIDENCE OF INDEBTEDNESS
15 PURSUANT TO A.R.S. § 40-302(A).

DOCKET NO. W-03512A-07-0362

16 **REBUTTAL TESTIMONY**
17 **OF**
18 **ROBERT T. HARDCASTLE**

1 **I. INTRODUCTION AND QUALIFICATIONS.**

2 **Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND TELEPHONE**
3 **NUMBER.**

4 A. Robert T. Hardcastle, 3101 State Rd., Bakersfield, California 93308. My telephone
5 number is (661) 633-7526.

6 **Q. ARE YOU THE SAME ROBERT HARDCASTLE THAT FILED DIRECT**
7 **TESTIMONY IN THIS MATTER?**

8 A. Yes, my direct testimony was filed on November 7, 2007 in support of Pine Water
9 Company's ("PWCo" or the "Company") application in this docket.

10 **Q. HAVE YOU REVIEWED MR. CHAVES' AND MR. SCOTT'S**
11 **RESPONSIVE TESTIMONIES ON BEHALF OF STAFF?**

12 A. Yes.

13 **Q. HAVE YOU REVIEWED THE INTERVENERS', MR. GREER'S AND**
14 **MR. KRAFCZYK'S, DIRECT TESTIMONIES?**

15 A. Yes.

16 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

17 A. Generally, to respond to the testimonies by Staff and the two interveners.

18 **Q. PLEASE SUMMARIZE THE COMPANY'S REBUTTAL TO THE**
19 **TESTIMONIES FILED BY STAFF AND THE INTERVENERS.**

20 A. Regarding Staff's testimony, it must be emphasized that Staff continues to
21 recommend approval of the Application and agrees that having its
22 recommendations track the statutory language is appropriate. We do find Staff's
23 advance prudence requirements unusual in this docket but, after consultation with
24 Staff, understand where they are coming from and will work with them towards the
25 common goal of finding long-term, continuous water supplies for our customers.
26 We also completely disagree with Staff that the K2 Agreement is a loan

1 transaction. We are in full agreement with Staff that the Commission need not and
2 should not attempt to characterize the transaction as anything other than “evidence
3 of indebtedness.”

4 Regarding the testimony of the Interveners, we are disappointed that they
5 have chosen to ignore the clear cautions by the Judge and at least two
6 Commissioners regarding the Commission’s authority and the scope of this
7 proceeding. We are not here to determine whether PSWID should or should not
8 have entered into the K2 Agreement with PWCo, and if so, on what terms. Nor are
9 we here so the Commission can make the Company’s operational decisions based
10 on objections by customers who seem to think they know better than we do how to
11 operate this water company. We are simply here, in an abundance of caution as a
12 regulated water provider, to obtain two narrow approvals related to our decision to
13 pursue the K2 well project. With respect to those approvals, the Interveners have
14 presented no credible evidence to support their opposition to our efforts to bring
15 more water to our customers.

16 **II. REBUTTAL TO STAFF TESTIMONIES.**

17 **A. Testimony by Staff Engineer.**

18 **Q. DO YOU HAVE ANY REBUTTAL TO THE TESTIMONY BY THE STAFF**
19 **ENGINEER, MARLIN SCOTT, JR.?**

20 **A.** I find it somewhat unusual that Mr. Scott is testifying now in this docket to
21 information Staff wants to see if the K2 well project is later sought for inclusion in
22 rate base. *See* Scott Responsive Testimony at 3.

23 **Q. WHY DO YOU FIND THIS TO BE UNUSUAL?**

24 **A.** Because the prudence of the K2 well project is not at issue in this proceeding. The
25 well does not even exist yet. In addition, Staff does not appear to be seeking any
26 affirmative relief in this docket with respect to this issue. The testimony seems to

1 be merely "advisory" in nature. *Id.*

2 **Q. HAS THE COMPANY DISCUSSED THIS MATTER WITH STAFF?**

3 A. Yes, and those discussions confirmed my understanding that Staff is trying to help
4 the Company by identifying the information it would like to see to evaluate the
5 prudence of the K2 well project in a future rate case. Further, Staff has informed
6 us that they have discussed the opinion letter with ADWR, and that ADWR is
7 willing to review test well data and render an opinion regarding the likely "long-
8 term continuous capacity" of the K2 well.

9 **Q. DOES THIS MEAN YOU HAVE TO COMPLETE THE WELL PROJECT**
10 **BEFORE YOU CAN OBTAIN THIS LETTER FROM ADWR?**

11 A. Not to my understanding, and obviously we are not going to invest a million
12 dollars or more in a well project only to have ADWR determine with hindsight that
13 it does not meet Staff's "long-term continuous capacity" requirement.

14 **Q. THEN HOW WILL THIS REQUIREMENT OF STAFF'S BE FULFILLED?**

15 A. Based on my discussions with Staff, I understand Staff would simply like PWCo to
16 supply the information from the test well to ADWR. ADWR will then evaluate
17 that information and provide the Company its opinion whether a production well at
18 the K2 site is likely to provide a "long-term continuous" supply.

19 **Q. DOES THE COMPANY HAVE ANY PROBLEM WITH THIS PROCESS?**

20 A. Not really. Even though there is no clear requirement that the Company take this
21 step, since the Company and PSWID will be evaluating the test well data to
22 determine whether a production well at the K2 site will result in an estimated
23 sustainable yield of 150 gpm, I do not believe Staff's desire for an ADWR opinion
24 letter is overly burdensome.

25

26

1 **B. Testimony by Staff's Public Utility Analyst.**

2 **Q. DO YOU HAVE ANY CONCERNS OVER THE TESTIMONY BY**
3 **MR. CHAVES?**

4 A. This testimony also results in a somewhat unusual situation. Staff and the
5 Company appear to have differing points of view concerning the nature of the
6 transaction contemplated in the K2 Agreement. Nevertheless, both parties agree
7 that the issue is not germane to the relief sought by PWCo in this docket. *See*
8 Chaves Responsive Testimony at 3-4 (adopting PWCo's revised Staff
9 recommended conditions for approval).

10 **Q. HOW DOES THE COMPANY AND STAFF DIFFER OVER THE NATURE**
11 **OF THE TRANSACTION?**

12 A. In PWCo's September 26, 2007 Response to Staff Report, the Company expressed
13 disagreement that, under the K2 Agreement, PSWID is lending and PWCo is
14 borrowing money.

15 **Q. HOW DO YOU CHARACTERIZE THE TRANSACTION BETWEEN THE**
16 **COMPANY AND THE PSWID UNDER THE K2 AGREEMENT?**

17 A. PSWID has agreed to make an investment to further its efforts to find long-term
18 water supplies in the Pine-Strawberry area by drilling a test well at the K2 site.
19 The funds provided by PSWID will be paid directly to the well drillers out of an
20 escrow fund, and if the test well does not lead to a production well being drilled on
21 the site, the test well will be in the sole possession of the PSWID. If the test well is
22 successful, i.e., results in an estimated sustainable yield of 150 gpm, PWCo will
23 invest up to an additional \$1 million to drill and interconnect a production well and
24 additional storage to the PWCo system. Thereafter, if the Commission allows the
25 Company a return on and of the costs of the K2 well project through rate base
26 treatment, PWCo will return PSWID's investment along with a return on that

1 investment.

2 **Q. TO YOUR KNOWLEDGE, DOES PSWID SHARE THIS VIEW OF THE K2**
3 **TRANSACTION?**

4 A. Yes, definitely, as reflected in the *JOINT WELL DEVELOPMENT AGREEMENT:*
5 *The District's Investment to Locate a New Dependable Water Source*, a document
6 prepared by the PSWID at our request. A copy of this document is attached to my
7 rebuttal testimony as **Hardcastle Rebuttal Exhibit 1**.

8 **Q. DOES THE COMMISSION NEED TO RESOLVE THE ISSUE OF HOW**
9 **THE K2 TRANSACTION IS CHARACTERIZED IN THIS DOCKET?**

10 A. Not in our view. As discussed in my direct testimony (at page 4), we have sought
11 Commission approval of our contingent obligation to return PSWID's investment if
12 certain conditions come to fruition in the future. It is more than sufficient for the
13 Commission to issue approval of an "other evidence of indebtedness." Again,
14 despite our differing views, Staff and the Company are in agreement on this point.
15 See Chaves Responsive Testimony at 3-4 (adopting PWCo's revised Staff
16 recommended conditions for approval).

17 **Q. DOES THE COMPANY ACCEPT STAFF'S RECOMMENDATIONS IN**
18 **THIS DOCKET?**

19 A. Yes, as revised in PWCo's Response to Staff Report and accepted by Staff, and
20 subject to the differing points of view discussed in this rebuttal testimony.

21 **III. REBUTTAL TO INTERVENERS' TESTIMONIES.**

22 **Q. DOES THE COMPANY HAVE CONCERNS WITH RESPECT TO THE**
23 **DIRECT TESTIMONY FILED BY MR. GREER AND MR. KRAFCZYK?**

24 A. Yes. The testimonies filed by these interveners suffer from two fundamental flaws.
25 First, Mr. Krafczyk and Mr. Greer have each filed testimony that goes beyond the
26

1 scope of this proceeding. Second, their testimonies make sweeping allegations
2 concerning matters over which the interveners lack personal knowledge.¹

3 **Q. WHY DO YOU BELIEVE THAT THEIR TESTIMONIES GO BEYOND**
4 **THE SCOPE OF THESE PROCEEDINGS?**

5 A. For example, Mr. Greer wants the Commission to address whether conflicts of
6 interest existed before as well as during and after the K2 Agreement was
7 negotiated. Mr. Krafczyk wants the Commission to address PSWID's legal
8 authority to enter into the K2 Agreement, whether the PSWID Board can bind
9 future boards, whether it can put funds in escrow, whether it had sufficient
10 information and whether it has assumed too much risk. Setting aside that these
11 appear to me to be largely legal issues, these matters have nothing to do with
12 whether or not the Commission should approve the requested encumbrance and
13 evidence of indebtedness.

14 Apparently Mr. Krafczyk and Mr. Greer feel it is okay to ignore Judge
15 Nodes who indicated that the PSWID is "an individual government entity that has
16 been formed and the Commission does not have the authority to tell that entity
17 what to do." Transcript, October 26, 2007, at 33-34. *See also* Transcript at 43.
18 Judge Nodes went even further, in responding to Mrs. Krafczyk during public
19 comment, and explained in explicit terms that "frustrations" with the PSWID are
20 "outside the scope of this case and even the Commission's authority to act on what
21 that entity's actions are." *Id.* Chairman Gleason and Commission Mundell echoed
22 Judge Nodes' view that the proceeding does not involve telling PSWID how and
23 where to spend its money or what else it should do. *Id.* at 44-45, 59.

24
25 ¹ PWCo has submitted data requests to the Interveners seeking to discover whether they actually have personal
26 knowledge to support their testimony. However, given the short interlude between the filing of the Interveners'
testimonies and the Company's rebuttal, responses have not yet been received. PWCo will supplement and/or amend
this testimony if necessary after receipt and review of the discovery responses.

1 **Q. DO YOU HAVE AN OPINION AS TO WHY THE INTERVENERS ARE**
2 **RAISING THESE ISSUES DESPITE THE CAUTIONARY COMMENTS BY**
3 **THE PRESIDING JUDGE?**

4 A. I do. The interveners are opposed to the K2 well project, and are looking to
5 leverage every possible opportunity to paint BUI and myself as evil-doers. In
6 effect, these opposition parties not only oppose BUI, but regulation by the
7 Commission in general. Mr. Krafczyk, Mr. Greer and others have a right to their
8 opinion and to pursue their positions in the proper forums. But in this case, while it
9 is unfortunate that Mr. Greer and Mr. Krafczyk have intervened in an effort to
10 expand the issues before the Commission, that effort should fail.

11 **Q. WHAT ABOUT YOUR CONCERN THAT THE INTERVENERS ARE**
12 **TESTIFYING TO MATTERS OVER WHICH THEY DO NOT HAVE**
13 **PERSONAL KNOWLEDGE?**

14 A. Mr. Greer testifies that the K2 site is insufficient and that we do not have adequate
15 access. Mr. Greer has never requested permission to be on the site and he has
16 never consulted with PWCo or its representatives regarding our plans for the K2
17 well project. I do not see how he can offer such testimony.

18 **Q. ARE THESE ISSUES EVEN RELEVANT TO THESE PROCEEDINGS?**

19 A. I am not a lawyer, but not in my view. As I explained in my prior testimony, in an
20 abundance of caution we have sought two narrow approvals from the Commission
21 related to the K2 Agreement. While we understand the Commission's desire that
22 PWCo locate additional water supplies, we simply do not believe it is the role of
23 the Commission to preempt the operational decisions being made by PWCo in its
24 efforts to locate long-term solutions to the region's chronic water supply problems.

25
26

1 **Q. DOES MR. KRAFCZYK OFFER TESTIMONY THAT IS SIMILARLY**
2 **PROBLEMATIC?**

3 A. In my view, yes. Mr. Krafczyk asks the Commission to evaluate whether the
4 property subject to the requested encumbrance is of sufficient value, and like
5 Mr. Greer, he attempts to offer testimony regarding the adequacy of the site and
6 our rights of access. First, as I explained in my direct testimony, the utility
7 property to which the lien will attach does not even exist yet, and I am not aware of
8 any appraisal of the K2 site to support Mr. Krafczyk's testimony. On what basis
9 then is Mr. Krafczyk offering this testimony? The answer appears to be—none
10 whatsoever.

11 Second, as with Mr. Greer, I do not see how Mr. Krafczyk can possibly have
12 personal knowledge concerning the K2 site and our efforts to develop it as a well
13 site. Third, as I testified to earlier, these matters appear to the Company to be
14 outside the scope of this proceeding to approve an encumbrance and evidence of
15 indebtedness.

16 **Q. ARE THERE ANY ASPECTS OF THE INTERVENERS' TESTIMONIES**
17 **THAT YOU BELIEVE ARE GERMANE TO THIS PROCEEDING?**

18 A. Mr. Krafczyk testifies that it is "clear" that PWCo does not have the credit
19 worthiness or financial capacity to return PSWID's investment in the K2 well
20 project. I agree that this is something the Commission needs to consider in
21 connection with the approval of an evidence of indebtedness.

22 **Q. IS MR. KRAFCZYK CORRECT?**

23 A. No, again, it appears that Mr. Krafczyk is testifying to matters outside his personal
24 knowledge. For one thing, Mr. Krafczyk claims to base his testimony on his
25 review of "publicly available records" but he fails to identify those records or the
26 information he has relied upon. He is also wrong. The Company's shareholder,

1 BUI, and the shareholder's shareholder and affiliates are well capitalized. I am
2 absolutely confident that we could return PSWID's investment through an infusion
3 of paid-in-capital and/or debt.

4 **Q. IS MR. KRAFCZYK RIGHT THAT PWCO WILL NEED A**
5 **"SUBSTANTIAL RATE INCREASE"?**

6 A. Not to return PSWID's investment. According to Staff's TIER and DSC
7 calculations, the Company will actually be able to meet all of its obligations from
8 existing revenues. Staff Report at 3. However, if PWCo invests capital in the K2
9 well project and that project is determined to be used and useful, we expect that
10 rates will have to be increased. This should be obvious. If we are going to invest
11 in finding additional water supplies, our ratepayers are going to have to pay for a
12 recovery on and of that investment through rates. That is how regulation works.

13 **Q. DO YOU HAVE ANY OTHER RESPONSE TO THE INTERVENERS'**
14 **TESTIMONY?**

15 A. There are two other issues I would like to address—the location of the K2 well in
16 Strawberry versus Pine and the alleged impact of the K2 well on Fossil Creek and
17 Fossil Springs.

18 **Q. EXCUSE ME, MR. HARDCASTLE, BUT AREN'T THESE OPERATIONAL**
19 **ISSUES OUTSIDE THE SCOPE OF THESE PROCEEDINGS?**

20 A. Yes, as I testified earlier, we do not believe it is the Commission's role or right to
21 direct where the Company locates a deep well. Nevertheless, there has been so
22 much misinformation on these two issues that I would like to respond.

23 **Q. OKAY, PLEASE RESPOND.**

24 A. First, PWCo does not own a satisfactory well site in Pine and despite his claim that
25 we should drill there, Mr. Greer does not offer any evidence to support his
26 allegations regarding our choice of a well site. In contrast, PSWID and the

1 Company have been studying the matter for several years. Based on the
2 information that has been gathered, and after consideration of a number of factors,
3 we have exercised our individual discretions and concluded that the K2 site is the
4 place where we want to continue our collective efforts to find more water. Mr.
5 Greer is free to disagree, but his disagreement does not provide any basis for the
6 Commission to deny the requested approvals in this docket.

7 Second, Mr. Greer offers nothing more than his bare allegation and appears
8 to be speculating. In our view as a water provider in the area for more than a
9 decade now, and based on the volume of water that would come from a successful
10 deep well on the K2 site, we believe the impact on Fossil Creek or Fossil Springs
11 would be not only negligible, but essentially immeasurable.

12 **Q. DO YOU HAVE ANYTHING ELSE TO ADD TO YOUR REBUTTAL**
13 **TESTIMONY, MR. HARDCASTLE?**

14 **A.** Just that we again urge the Commission to move quickly and grant the requested
15 approvals. For years we have been told by just about everyone interested that it is
16 our responsibility to make the decisions to try to bring more water to the
17 communities we serve. Okay, we accept that responsibility, and while we can
18 agree to disagree about the past, no one can legitimately dispute that we are now
19 trying to find more water. At present, while we would like to already be out
20 drilling the K2 test well, individuals like the Interveners are attempting to hijack
21 the regulatory process to further their opposition to BUI, the current PSWID Board
22 and/or regulation in general.

23 In the end, we are doing exactly what this Commission ordered us to do in
24 Decision No. 67823--which is to work with local entities like PSWID to find more
25 water. The success or failure of that effort falls on us and, while I understand that
26 the Commission must consider the concerns of the citizens they represent, there

1 comes a time when politics has to stand aside. I respectfully suggest that time is
2 now.

3 **Q. DOES THAT CONCLUDE YOUR DIRECT TESTIMONY?**

4 A. Yes.

5

2005726.1/75206.015

6

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

26

Docket No: W-03512A-07-0362

Hardcastle Rebuttal Exhibit 1

THE JOINT WELL DEVELOPMENT AGREEMENT
The District's Investment to Locate a
New Dependable Water Source

1. The Pine/Strawberry Water Improvement District's (PSWID) entered into the Joint Well Development Agreement in furtherance of its stated mission:

[T]o represent the interests of the communities [of Pine and Strawberry] and to secure long term and reliable sources of water for the communities. To accomplish this we are to: 1) Investigate current and potential sources of water as well as the costs associated with maintaining or expanding present and potential sources. 2) Formulate a plan or plans for improving present water sources of the communities. 3) Formulate a plan or plans for funding such improvements. 4) Implement and formulate plans as necessary to provide long-term available water to communities. PSWID's Mission Statement

2. Since PSWID's formation, PSWID Boards have regularly authorized expenditures on investigations and studies to enhance the potential for improving and supplementing present water sources available to the Pine and Strawberry communities, including investing capital in the joint development and monitoring of the Strawberry Borehole.

3. The Joint Well Development Agreement represents another cooperative effort by PSWID to determine where a new dependable water source can be developed. Under the Agreement:

- a. PSWID is pursuing its mission of enhancing the potential for improving and supplementing water sources available to the Pine and Strawberry communities by investing \$300,000 to fund drilling a deep test well into the R aquifer and conducting pump tests and other evaluations of the test well.
- b. PWCo is committing to either a) convey the project to PSWID, including the well site, or b) if the test well demonstrates there is a likelihood that 150 gpm or more of sustainable yield can be produced at the site, to develop and place in service a production well at the site (something PSWID lacks funding to accomplish independently).

4. The Joint Well Development Agreement does not involve a "loan" to PWCo.

- a. No money is transferred or given to PWCo. Funds are placed into escrow, where PSWID retains control over their expenditure. All funds will be paid to third parties (not PWCo) for work performed in furtherance of the Joint Well Development Agreement.
- b. PWCo, as well as all other members of the public, will have access to the pump test and well driller data developed from PSWID's investment. From that data, PSWID and PWCo will determine whether there is a likelihood that a sustainable yield of 150 gpm or more form the K2 site.
- c. If the work halts at any time before a production well is placed in service, PSWID will receive the improved K2 site at no further cost to PSWID.¹
- d. However, if the production well is constructed and placed both in service and in PWCo's rate base, then PWCo becomes obligated to return PSWID's capital investment with a reasonable return thereon.

5. Out of an abundance of caution PWCo seeks Commission approval to incur this contingent "indebtedness" pursuant to A.R.S. §40-302(A).

6. PSWID has limited funds and limited funding sources. It does not have sufficient funds to develop a production well on its own.

7. PSWID owns no land upon which it can drill a test well or a production well. If it must pay to acquire a well site or access, the amount available for drilling and testing is reduced.

8. The Joint Well Development Agreement addresses and resolves these limitations by partnering with PWCo on an existing site, with a good hydrologic upside and located in proximity to the existing water distribution system that services both the Pine and Strawberry Communities.

¹ Instead of accepting the improved wellsite, PSWID, in its sole discretion, may elect to have PWCo abandon the well by encasing and sealing it consistent with ADWR rules