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Arizona Corporation Commission
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AZ CORP COMMISSION
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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 OF
11 ITS PLANT AND SYSTEM PURSUANT TO
12 A.R.S. §40-285(A); AND (2) ISSUE EVIDENCE
13 OF INDEBTEDNESS PURSUANT TO A.R.S.
14 §40-302(A).

DOCKET NO. W-03512A-07-0362

BRIEF OF INTERVENORS

15 COMES NOW FRED KRAFCZYK AND MICHAEL GREER, Intervenor in the above captioned and
16 numbered matter, by and through their attorney undersigned, and hereby submit their Brief concerning
17 the legal issues raised by and during the foregoing proceeding.

18 I.

19 DOES THE ACC HAVE THE JURISDICTION TO CONSIDER THE IMPACT UPON THE
20 PROPERTY OWNERS AND WELL OWNERS IN STRAWBERRY OF THE K2 WELL IF IT IS
21 CONSTRUCTED?

22 Article 15 Section 3 of the Constitution of the State of Arizona sets forth the Power of the Arizona
23 Corporation Commission, to wit:

24 3. Power of commission as to classifications, rates and charges, rules,
25 contracts, and accounts; local regulation

26 Section 3. The corporation commission shall have full power to, and shall,
27 prescribe just and reasonable classifications to be used and just and
28 reasonable rates and charges to be made and collected, by public service
29 corporations within the state for service rendered therein, and make
reasonable rules, regulations, and orders, by which such corporations shall
be governed in the transaction of business within the state, and may

1 prescribe the forms of contracts and the systems of keeping accounts to be
2 used by such corporations in transacting such business, and make and
3 enforce reasonable rules, regulations, and orders for the convenience,
4 comfort, and safety, and the preservation of the health, of the employees
5 and patrons of such corporations; Provided, that incorporated cities and
6 towns may be authorized by law to exercise supervision over public
7 service corporations doing business therein, including the regulation of
8 rates and charges to be made and collected by such corporations; Provided
9 further, that classifications, rates, charges, rules, regulations, orders, and
10 forms or systems prescribed or made by said corporation commission may
11 from time to time be amended or repealed by such commission.

12 This power has been further enhanced by the legislature through the adoption of a number of statutes,
13 to wit:

14 ARS Section 40-285A

15 40-285. Disposition of plant by public service corporations; acquisition of
16 capital stock of public service corporation by other public service
17 corporations

18 A. A public service corporation shall not sell, lease, assign, mortgage or
19 otherwise dispose of or encumber the whole or any part of its railroad, line,
20 plant, or system necessary or useful in the performance of its duties to the
21 public, or any franchise or permit or any right hereunder, nor shall such
22 corporation merge such system or any part thereof with any other public
23 service corporation without first having secured from the commission an
24 order authorizing it so to do. Every such disposition, encumbrance or
25 merger made other than in accordance with the order of the commission
26 authorizing it is void.

27 ARS Section 40-302A:

28 40-302. Order authorizing issuance of stocks, bonds or other evidences of
29 debt; hearing on application to issue; amount of issue; issuance of short
30 term notes without commission order; capitalization of certain items
31 prohibited; accounting for proceeds of issues

32 A. Before a public service corporation issues stocks and stock certificates,
33 bonds, notes and other evidences of indebtedness, it shall first secure from
34 the commission an order authorizing such issue and stating the amount
35 thereof, the purposes to which the issue or proceeds thereof are to be
36 applied, and that, in the opinion of the commission, the issue is reasonably
37 necessary or appropriate for the purposes specified in the order, pursuant
38 to section 40-301, and that, except as otherwise permitted in the order,
39 such purposes are not, wholly or in part, reasonably chargeable to
40 operative expenses or to income. Before an order is issued under this
41 section, notice of the filing of the application for such order shall be given
42 by the commission or the applicant in such form and manner as the
43 commission deems appropriate. The commission may hold a hearing, and

1 make inquiry or investigation, and examine witnesses, books, papers and
2 documents, and require filing data it deems of assistance.

3 ARS section 40-321:

40-321. Power of commission to determine adequacy of service rendered by public service corporation; enforcement by order or regulation; duty of compliance by corporation; surety; utility surety fund

A. When the commission finds that the equipment, appliances, facilities or service of any public service corporation, or the methods of manufacture, distribution, transmission, storage or supply employed by it, are unjust, unreasonable, unsafe, improper, inadequate or insufficient, the commission shall determine what is just, reasonable, safe, proper, adequate or sufficient, and shall enforce its determination by order or regulation.

B. The commission shall prescribe regulations for the performance of any service or the furnishing of any commodity and upon proper demand and tender of rates, the public service corporation shall furnish the commodity or render the service within the time and upon the conditions prescribed.

C. If, after notice and an opportunity to be heard, the commission finds that a public service corporation is in default of the terms and conditions of an order of the commission that requires a performance bond, irrevocable letter of credit or other surety, and the commission exercises its rights under the bond, letter or other surety, the commission shall deposit all monies received as a result of exercising the rights in the utility surety fund established by subsection D of this section.

D. The utility surety fund is established consisting of monies received by the commission pursuant to subsection C of this section. Monies in the utility surety fund shall be administered by the commission for the benefit of the customers of the public service corporation who have incurred a loss of services or commodities or for deposit support pursuant to this section. Monies in the fund are continuously appropriated to the commission and do not revert to the state general fund pursuant to section 35-190.

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ARS Section 40-322

40-322. Regulation of public service corporations; standards of service; measurement standards; inspections by commission

A. The commission may:

1. Ascertain and set just and reasonable standards, classifications, regulations, practices, measurements or service to be furnished and followed by public service corporations other than a railroad.
2. Ascertain and fix adequate and serviceable standards for the measurement of quantity, quality, pressure, initial voltage or other condition pertaining to the supply of the product, commodity or service furnished by such public service corporation.
3. Prescribe reasonable regulations for the examination and testing of the product, commodity or service and for the measurement thereof.
4. Establish reasonable rules, regulations, specifications and standards to secure the accuracy of all meters and appliances for measurements.
5. Provide for the examination and testing of any and all appliances used for measurement of any product, commodity or service of any such corporation.

B. The commission, its officers and employees may enter upon any premises occupied by a public service corporation, for the purpose of making the examinations and tests and exercising any of the other powers provided for in this article, and may set up and use on the premises any apparatus and appliances necessary therefore. The agents and employees of the public service corporation may be present at the making of the examinations and tests.

C. Any consumer or user of any product, commodity or service of a public service corporation may have any appliance used in the measurement thereof tested upon paying the fees fixed by the commission, the fee to be paid by the consumer or user at the time of his request, but to be paid by the corporation and repaid to the consumer or user if the appliance is found defective or operates to the disadvantage of the consumer or user.

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ARS Section 40-361

40-361. Charges by public service corporations required to be just and reasonable; service and facilities required to be adequate, efficient and reasonable; rules and regulations relating to charges or service required to be just and reasonable

1 A. Charges demanded or received by a public service corporation for any
2 commodity or service shall be just and reasonable. Every unjust or
unreasonable charge demanded or received is prohibited and unlawful.

3 B. Every public service corporation shall furnish and maintain such
4 service, equipment and facilities as will promote the safety, health,
5 comfort and convenience of its patrons, employees and the public, and as
6 will be in all respects adequate, efficient and reasonable.

7 C. All rules and regulations made by a public service corporation affecting
8 or pertaining to its charges or service to the public shall be just and
reasonable.

9 The power and authority of the Corporation Commission is derived from the Constitution and Statutes of
10 the State of Arizona. *Tonto Creek Estates Homeowners Association v. Arizona Corporation
11 Commission, 177 Ariz. 49, 864 P.2d 1081 (Ct. App. 1993)*. The question remaining is what evidence
12 may be considered by the Corporation Commission in reaching its decision concerning the encumbering
13 of assets and the issuance of the evidence of indebtedness. It is the position of the intervenors that it
14 may hear all evidence which the Corporation Commission deems relevant and material to making its
15 decision. It is not and cannot be limited by any action of the legislature. The Corporation Commission
16 is charged by the state constitution with making rules, regulations and orders by which public service
17 corporations shall be governed in the transaction of business within the state. *State v. Tucson Gas,
18 Electric Light and Power Company, 15 Ariz. 294, 138 P. 781 (1914)*.

19 The Corporation Commission is exercising powers which are delegated to it by the Constitution
20 and Statues of the State of Arizona. In that capacity, it can and does conduct hearings concerning
21 matters brought before it, looking at such matters in light of the public interest of the citizens of the
22 state. The Corporation Commission, within the areas or arenas where it has been granted power and
23 authority to regulate, does have plenary power to do so. *Jennings v. Woods, 194 Ariz. 314, 982 P.2d
24 274 (S.Ct. 1999); Tucson Electric Power Company v. Arizona Corporation Commission, 132 Ariz.
25 240, 645 P.2d 231 (S. Ct 1982) see also Kilpatrick v. Superior Court 105 Ariz. 413, 466 P.2d 18(1970)*

26 . The Corporation Commission supervises and regulates all relations between a corporation and the
27 public. *Corporation Commission v. Consolidated Stage Company, 63 Ariz. 257, 161 P.2d 110 (1945)*.
28 The Corporation Commission has the exclusive power as far as regulations pertaining to public service
29 corporations. *Corporation Commission v. Pacific Greyhound Lines, 54 Ariz. 159, 94 P.2d 443 (1939)*.

1 To regulate the relationship between Pine Water Company and the public the Corporation Commission
2 must hear evidence of the impact of Pine Water Company's actions on the public.

3 The public interest must be at the forefront of the regulatory process. It has long been held in this
4 state that:

5 The Commission is required to use these powers to regulate public service
6 corporations in the public interest. Southern Pac. Co. v. Arizona Corp.
7 Comm'n, 98 Ariz. 339, 342, 404 P.2d 692, 694 (1965); see generally
8 Engelby, supra, at 245. Thus, the founders' intent and the text gave the
9 elected Commission a strong role in protecting the public interest through
10 regulation of public service corporations. See Engelby, supra, at 244-45;
11 see also Making the Arizona Constitution, supra, at 90-91. ***Arizona***
12 ***Corporation Commission v. State, 171 Ariz. 286 291, 292, 830 P.2d 807***
13 ***(S.Ct. 1992)***

14 The Corporation Commission does, without a doubt, have jurisdiction over the public service
15 companies which are subject to its regulation. If for no other reason than the protection of the
16 Strawberry Water Company, the Commission should be able to look at the impact this proposed K2 well
17 may have upon wells located in its vicinity, which would include wells of the Strawberry Water
18 Company. The Commission needs to protect the public served by the regulated public service
19 corporations, and it has a concomitant obligation to protect the public interest in general from the actions
20 of a regulated public service corporation. There is neither constitutional provision nor provision of state
21 law adopted by the legislature which precludes the Commission from looking at the impact of the K2
22 well upon the other wells in the Strawberry and Pine areas. ***See Yuma Gas, Light and Water Company***
23 ***v. City of Yuma, 20 Ariz. 153, 178 P. 26 (1919)***

24 The question of the public interest is also paramount in the determination of the granting or
25 amending of a Certificate of Convenience and Necessity granted to any public service corporation.
26 ***James P. Paul Water Company v. Arizona Corporation Commission, 1637 Ariz. 426, 671 P.2de 404***
27 ***(S.Ct. 1983), Arizona Corporation Commission v. Arizona Water Company, 111 Ariz. 74, 523 P.2d***
28 ***505 (S.Ct. 1974)***. The public interest is a matter to be considered by and defined by the Commission.
29 To do it properly, in this instance, will require that the Commission receive all evidence as to the impact
of the proposed K2 Well before it makes a determination as to whether or not it should approve Pine
Water Company entering into the contract or issuing evidence of indebtedness.

1 A fair question to also be raised is whether or not Pine Water Company is prepared to act under
2 this agreement. There has been no judicial determination made as to the capacity of the District to enter
3 into this agreement. There is limited engineering. The definitive site plan and easements for access to
4 the site are issues in need of resolution, and finally, there is no guarantee that Pine Water Company or its
5 parent corporation will in fact ever repay the amount borrowed, given the number of exceptions set forth
6 in the agreement attached to their application.

7 Staff has argued that the burden lies on the intervenors or on the citizens of Strawberry to present
8 evidence of the impact. In the fulfillment of its obligations to protect the public interest, the intervenors assert
9 that it should be the burden of Pine to show that they will not have an impact upon the water availability in
10 Strawberry.

11 II.

12 PINE WATER COMPANY SHOULD NOT BE ALLOWED TO ENCUMBER A PORTION OF ITS
13 ASSETS.

14 Pine Water Company has come before the Corporation Commission requesting permission to encumber
15 a portion of its assets, more particularly the K2 wellsite. In fact it is proceeding with the transaction,
16 only making a contingency allowance for the possibility of the lack of approval by the Corporation
17 Commission. {See Exhibit A attached hereto, the escrow instructions regarding the transaction which
18 have been approved by the Pine Strawberry Water Improvement District}. Further, Pine is still having
19 difficulty with the use of the easements to enter into the property.

20 In addition, this property is presently held by an entity other than Pine Water Company, so
21 without a conveyance to Pine Water Company, Pine has nothing to encumber.

22 PINE WATER COMPANY SHOULD NOT BE ALLOWED TO ISSUE EVIDENCE OF
23 INDEBTEDNESS.

24 The principal reason for now allowing the company to issue the evidence of indebtedness is that the
25 lender of the money lacks the legal capacity and authority to enter into this agreement with Pine Water
26 Company, and the indebtedness would violate the State Constitution, thus the evidence of indebtedness
27 would not be a viable instrument.

28 THE PROPOSED CONTRACT IS CONSTITUTIONALLY DEFICIENT AND IT REQUIRES THE
29 PARTIES TO ENGAGE IN ACTS NOT ALLOWED THE ARIZONA CONSTITUTION.

1 The Corporation Commission must consider the public interest in making its determination. Pine has
2 presented an unconstitutional contract with a party which lacks the capacity to enter into the contract.
3 So, in essence the contract would be void. There are two provisions of the Constitution of the State of
4 Arizona which must be considered in making this review Article 9 Section 7 which prohibits the loaning
5 of the credit of a municipal corporation to a private entity or the making of a donation or grant to a
6 private entity and : Article 9 Section 10 which prohibits a municipal corporation from loaning funds to a
7 public service corporation. Both sections preclude the Pine Strawberry Water Improvement District
8 from entering into this agreement.

9 Article 9 Section 7 clearly states that:

10 Neither the State, nor any county, city, town, municipality, or other
11 subdivision of the state shall ever give or loan its credit in the aid of, or
12 make any donation or grant, by subsidy or otherwise to any individual,
association or corporation . . .

13 The purpose of this constitutional provision is to prevent governmental bodies from depleting the public
14 treasury by giving advantages to special interests. *Wistuber v. Paradise Valley Unified School District,*
15 *141 Ariz. 346 (S.Ct. 1984)* While it is true that the Court has carved out exceptions allowing for the use
16 of certain funds, such as bond proceeds to be used in public private partnerships, that is not the case
17 before the Commission here. In this case, the District is taking money from its general fund, which was
18 raised through taxation of its residents, and turning this over to the private concern, Pine Water
19 Company, in exchange for a possibility of getting the money back if a successful test Well is drilled.
20 The consideration being received by the District is contingent at best. This hardly meets the balancing
21 test required to exempt the expenditure of public funds from this constitutional provision which requires
22 at the least, the governmental authority be paid some reasonable consideration. *Cf State v. Superior*
23 *Court, 159 Ariz. 307, 767 P.2d 30 (Ct. App. 1988); Wistuber v. Paradise Valley Unified School*
24 *District, 141 Ariz. 346 (S.Ct. 1984).* If what is being paid out by the District is in excess of what is
25 received in exchange by the District, the constitutional provision is being violated. In the face of that,
26 how can the Commission allow the Company to enter into a contract which will not survive
27 constitutional scrutiny.
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1 The test to be applied in making this determination was clearly set forth by the Arizona Supreme
2 Court in *Arizona Center for Law in the Public Interest v. Hassell*, 172 Ariz. 356, 837 P.2d 158 (S.Ct.
3 1992) wherein the Court Stated:

4 First, the reviewing court must be satisfied that a dispensation of public
5 funds or property serves a public purpose. Second, the reviewing court
6 must be satisfied that the dispensing public entity has received
7 "'consideration' which is not 'so inequitable and unreasonable that it
8 amounts to an abuse of discretion,' thus providing a subsidy to the private
9 entity."

10 The second state constitutional provision involved in this analysis is Article 9 section 10 of the
11 Constitution of the State of Arizona which states:

12 No tax shall be laid or appropriation of public money made in aid of any
13 church, or private or sectarian school, or any public service corporation.

14 This is an absolute prohibition. Clearly the agreement specifies that money is to be used from the
15 District, a municipal corporation, for the benefit of Pine Water Company, a public service corporation.
16 Here, the prohibition lies on both the public service corporation and the District. The Corporation
17 Commission cannot approve an agreement which directly violates the provisions of the Constitution of
18 the State of Arizona. Clearly the proposed drilling of the K2 Well is for the benefit of the Pine Water
19 Company. If the Well is successful the Pine Water Company gets the Well. If the well is not successful,
20 the District loses its money. It is an obvious violation of this constitutional provision.

21 III.

22 THE PEOPLE OF PINE WILL BE SUBJECT TO DOUBLE TAXATION AND THE PEOPLE OF
23 STRAWBERRY HAVE BEEN TAXED AND HAVE RECEIVED NO BENEFIT.

24 The people of Pine Arizona and Strawberry Arizona are being injured by this contract because it,
25 in essence, subjects them to paying twice for the same expense. First, all of the Pine Strawberry Water
26 Improvement District was taxed to raise the initial money. Then the money is to be used only for the
27 benefit of Pine Water Company, the territory of which only encompasses a portion of the District. So
28 those people located outside of the Certificated area of Pine Water Company are getting no benefit out of
29 the expenditure of the public funds to which they contributed. Second, the people in Pine, having first
been taxed to raise a portion of the initial money, will, if the project is successful and included in the rate
base of Pine Water Company, be repaying Pine Water Company so that the Water Company can repay

1 the District. Thus, they have paid twice for this project; once when the district gathered the money into
2 its treasury, and a second time when they are charged to pay it back to Pine.

3 In addition, if the project does not succeed, the people of the District have lost their money and
4 have, at best, the small parcel of property purportedly being encumbered, which encumbrance could be
5 subject to future legal challenges.

6 Finally, there is the question of the impact of the recent curtailment tariff adopted for the
7 Strawberry Water Company which essentially precludes wells in Strawberry from sending water to Pine
8 in time of water shortage. There is no clear provision in those tariff's exempting the K2 well, so it
9 would then be like the other two Pine Water Company owned wells in Strawberry, it could not be used
10 to supply water to Pine in times of shortage in Strawberry.

11 IV.

12 UNLAWFUL DELEGATION OF DISTRICT'S POWER AND CONTROL OVER FINANCES.

13 The District is a municipal corporation of the State of Arizona. As such it is subject to the laws
14 pertaining to the investment and use of publicly generated funds. In this proceeding the District is being
15 asked to surrender its public funds to an escrow and then such funds are paid out not pursuant to the sole
16 order of the District, but rather on a contingent basis, which requires the approval of Pine Water
17 Company. This constitutes an unlawful financial transaction for the district. It cannot surrender the
18 power and control over its monies to a third party.

19 The agreement for which approval is being sought requires that the District place funds into an
20 escrow account and said funds are to then later be paid out subject to the approval of Pine Water
21 Company. Section 4.2.1.4 of the Agreement. Thus, once the District has deposited the public monies in
22 this escrow, it loses control of these funds.

23 This arrangement is clearly contrary to the requirements of state law whereby the County
24 Treasurer is the District's Treasurer, *Arizona Revised Statutes Section 48-901* and in such capacity he is
25 limited to paying out general obligations of the District by *Arizona Revised Statutes Section 48-952* for
26 only certain purposes, none of the enumerated purposes contemplating a payment to an escrow fund or
27 the use of the general funds of the District to construct a test well. The County Treasurer can only
28 disburse monies in accordance with State law, *Arizona Revised Statutes Section 11-491*. Last the
29 money can only be disbursed by warrant, or a transfer approved by the governmental authority or as

1 provided by law. *Arizona Revised Statutes Section 11-493*. Nowhere in state law is the process of
2 paying the money into an escrow to be drawn out and paid by instruction of a public service corporation
3 set forth as an appropriate manner for the disbursement of public monies. Thus Pine Water Company
4 should not be allowed to enter into this contract.

5 **V.**

6 EASEMENT ISSUES TO THE K2 SITE

7 Clearly Pine Water Company is having issues regarding the access to the K2 Well site. Those problems
8 continue to this day. If these issues are not resolved, the public interest in both Pine and Strawberry is
9 being injured by the lack of resolution.

10 **VI.**

11 K2 IS A HIGH RISK AND PWC WOULD NOT DO IT WITHOUT THE MONEY FROM PSWID

12 How can it be in the public interest for the District to take the risk of investing its money in the K2 Well
13 when the risks of doing such a project are so great that Pine Water Company is unwilling to undertake
14 such a risk? While on one side, as testified by the Staff, it is a good deal because the company is not
15 investing its own money; the staff is overlooking its obligation to protect the public in the Pine and
16 Strawberry area.

17 **VII.**

18 PARCEL SIZE INSUFFICIENT FOR THE ACTIVITIES.

19 The testimony at the hearing, and at the public input session in Pine clearly points out that there
20 is insufficient space to conduct the well drilling operation on the site and to continue to operate the
21 facility. Again, the public safety is at stake when the well drilling operations exceed the allowable space
22 and water or other materials escape from the site and damage other property owners in the community.

23 **VIII.**

24 IMPACT OF BRENNINGER AND RICHIE CONFLICT OF INTEREST

25 *Arizona Revised Statutes Title 38 Article 8* sets forth the rules applicable to conflict of interest for
26 public officials and employees. John Brenninger worked for Pine Water Company prior to and perhaps
27 even during his tenure on the District Board. Jim Richie was engaged in business transactions of a
28 sizable nature with Pine Water Company or Brooke Utilities prior to and while a member of the Board
29 of the District. Clearly this, coupled with the other information presented herein, is indicative of

1 malfeasance in office or other conflicts of interest by these individuals. This is another reason why the
2 District lacked the capacity to enter into the contract with Pine Water Company.

3 It was reported that the information provided by Pine Water Company to the District, the peer
4 review reports concerning the K2 wellsite was not provided to all the District Board Members. Because
5 of that, the District Board did not have the full and complete information available to it in making its
6 decision. Again, the public interest was damaged by the actions of Pine Water Company and those with
7 whom it did business or engaged in business transactions or otherwise employed. These documents
8 were withheld in part by the actions of Mr. Richie

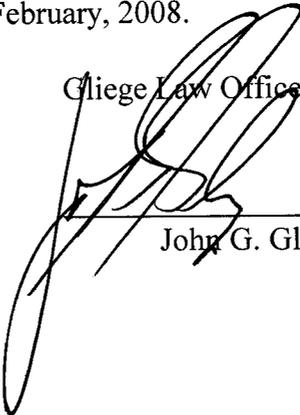
9 **IX.**

10 **CONCLUSION**

11 It is the position of the intervenors that the Arizona Corporation Commission should not approve
12 Pine Water Company entering into the K2 agreement nor issuing evidence of indebtedness regarding the
13 same. The transaction is fraught with legal issues and problems and it is directly in violation of the
14 Constitution of the State of Arizona. Therefore, it is respectfully requested that the Corporation deny the
15 request to approve entering into the contract and issuing evidence of indebtedness.

16 Respectfully submitted this 15th day of February, 2008.

17 Gliege Law Offices PLLC

18 
19 _____
20 John G. Gliege

21 Copies of the foregoing mailed/delivered
22 This 15th day of February, 2008 to:

23 Docket Control
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27 Mr. Dwight D. Nodes
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EXHIBIT A

ESCROW INSTRUCTIONS
(Joint Well JDWA)
(K2 Site)

THESE ESCROW INSTRUCTIONS ("Instructions") are entered into this ____ day of _____ 200__ ("Effective Date"), by and between Pine Water Company ("PWCo"), Pine-Strawberry Water Improvement District ("PSWID"), and Pioneer Funding Services, a division of Pioneer Title Agency, Inc. ("Escrow Agent").

RECITALS:

A. PWCo and PSWID have entered into that certain Joint Well Development Agreement dated May 1, 2007 (as amended, the "JDWA"). Pursuant to the JDWA, PWCo and PSWID agreed to a sequential development of a well site located in eastern Strawberry, Arizona, just south of Strawberry Creek, as more particularly described in the JDWA (the "Project").

B. Under Section 4 of the JDWA, PSWID has agreed to provide \$300,000 (the "PSWID Funds") to develop a test well and establish the sustainable yield, in accordance with the JDWA.

C. PWCo and PSWID desire to establish an escrow for the deposit of the PSWID Funds and to create a mechanism to govern the disbursement of PSWID Funds to pay contractors for their work on certain aspects of the Project.

D. Escrow Agent is willing to act as escrow agent for the PSWID Funds and to carry out its responsibilities hereunder.

AGREEMENT:

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which are mutually acknowledged, the parties agree as follows:

1. PSWID Funds.

(a) PSWID (i) having been notified in writing by PWCo that funding for the Project is available upon terms and conditions acceptable to PWCo, (ii) having been notified in writing by PWCo that title to the well site for the Project has been conveyed to PWCo, including easements within the well site for ingress, egress, maintenance, repair and replacement, (iii) having received from PWCo the executed Notice of Continuing Security Interest and Lien in favor of PSWID, expressly subject to any adverse final non-appealable decision of the Arizona Corporation Commission or court of law that the Continuing Security Interest and Lien is void and unenforceable, (iv) having received and approved the Project Plan and Project Budget submitted in writing by PWCo, and (v) having waived receipt of ACC approvals and recordation of the Notice of Continuing Security Interest and Lien as a precondition of depositing PSWID Funds with Escrow Agent, shall, within ten (10) days of its receipt of an executed original of these Instructions, deposit the PSWID Funds (\$300,000.00) with Escrow Agent.

(b) Escrow Agent shall invest all cash funds delivered and retained by Escrow Agent in one or more interest bearing account(s), with one or more federally insured banks with offices in Payson, Arizona satisfactory to PWCo and Escrow Agent. All interest earned on such sums shall be considered part of the PSWID Funds.

2. Disbursement of Escrowed Funds.

(a) Escrow Agent shall disburse the PSWID Funds upon written application in accordance with this Section 2 to pay for work performed pursuant to the JDWA. Escrow Agent shall not make any disbursements from the PSWID Funds for any purpose other than the following:

- (i) to pay a consultant hired by PSWID to coordinate and facilitate the design, construction, testing, and equipping of the test well in accordance with the JDWA;
- (ii) to pay a well driller hired by PWCo to drill, case, equip and test the test well in accordance with the JDWA;
- (iii) to pay material suppliers hired by PWCo for materials associated with the drilling, equipping and testing the test well in accordance with the JDWA;
- (iv) to pay a hydrologist hired by PWCo to make recommendations regarding the test well and regarding testing and to review and analyze test data in accordance with the JDWA;
- (v) to pay other contractors and suppliers hired by PWCo or PSWID to test, construct, and equip the test well in accordance with the JDWA;
- (vi) to return surplus funds to PSWID in accordance with Section 3, below;
- (vii) payment of fees and expenses in accordance with Section 4, below.

and then, for disbursements allowed under subsections (i) through (v) above, only after satisfaction of the conditions set forth below in this Section 2.

(b) The Escrow Agent shall be provided a written draw request (the "Draw Request") executed by the representatives of PWCo and PSWID designated under the JDWA at least three (3) business days before the date funds are to be disbursed. The Draw Request shall include the following:

- (i) A statement that in soliciting and contracting with the contractor the procedures and requirements set forth in Title 34, Chapters 2 and 3, Arizona Revised Statute have been applied and satisfied as if PSWID had contracted directly for the work or materials.
- (ii) Invoices and corresponding applications for payment of contractors, subcontractors and material suppliers stating in reasonable detail the

respective work performed or the materials supplied in connection with the Project or, if payment to the contractor, subcontractor or material supplier will be made in advance, invoices and corresponding applications for payment stating in reasonable detail the respective work to be performed or the materials to be supplied in connection with the Project;

- (iii) Statements of the amount due and payable to each such contractor, subcontractor and material supplier;
- (iv) Conditional lien waivers from all such contractors, subcontractors and material suppliers identified in any such invoices in a form complying with applicable law;
- (v) Unconditional lien waivers from all such contractors, subcontractors and material suppliers identified in any such invoices in form complying with applicable law for work performed and material supplied for which payment has been made in response to a previous invoice;
- (vi) Unconditional lien waivers in a form complying with applicable law upon request for final payment to the contractor, subcontractor or material supplier;
- (vii) An authorization for disbursement to Escrow Agent signed by PWCo or its authorized agent and by PSWID or its authorized agent stating (a) that the amounts requested for payment in the Draw Request are due and payable to the contractors, subcontractors and material suppliers and are for services and materials set forth in Section 2(a) above; and (b) that PWCo and PSWID jointly request the disbursement of the amounts stated in the Draw Request to the specified contractors, subcontractors and material suppliers.

(c) Upon Escrow Agent's receipt of the Draw Request and authorization to disburse signed by or on behalf of PWCo and PSWID, Escrow Agent shall disburse the funds requested in the Draw Request from the PSWID Funds. All checks shall be made payable to the contractor, subcontractor or material supplier to whom payment is due for work performed as set forth in the Draw Request. In no event shall any check be made payable directly to PWCo.

3. Delivery of Surplus Funds to PSWID. In the event the Project or the JDWA is terminated for any reason, or if PWCO has not contracted with a well driller to drill the test well by the later of March 1, 2008 or that date indicated and approved on the Project Plan, as it may be amended from time to time, or if the drilling of the test well is not commenced by the later of April 30, 2008 or that date indicated and approved on the Project Plan, as it may be amended from time to time, the parties shall notify Escrow Agent of such termination or inaction. Upon delivery of notice of such termination or inaction, no further draws shall be made on the PSWID Funds, and Escrow Agent immediately shall disburse the remaining PSWID Funds to PSWID.

4. Escrow Fees and Expenses. The fees and expenses associated with establishing and maintaining the escrow pursuant to these Instructions shall be paid to Escrow Agent out of the

PSWID Funds in accordance with the Schedule of Escrow Fees set forth on Exhibit "A" attached hereto.

5. Escrow Agent's Duties. Escrow Agent hereby accepts the duties imposed upon it by these Instructions, represents that it is fully empowered under any applicable laws and regulations to accept such duties, and agrees to perform such duties, but only upon and subject to the express terms and conditions set forth below:

(a) Escrow Agent shall be entitled to advice of counsel of its choosing concerning any controversy which may arise hereunder and Escrow Agent may pay reasonable compensation to all attorneys retained by it in such matters. Escrow Agent shall not be responsible for any loss or damage resulting from any action taken in good faith in reliance upon the opinion or advice of counsel.

(b) Escrow Agent shall incur no liability in acting upon any notice, request, consent, waiver, certificate, statement, opinion or other document which it shall reasonably believe to be genuine and to have been signed by the proper person and to have been prepared and furnished in connection with any of the provisions of these Instructions, and Escrow Agent shall be under no duty to make any investigation or inquiry as to any statement contained or matters referred to in any such instrument, but may accept and rely upon the same as conclusive evidence of the truth and accuracy of such statements.

(c) All monies held by Escrow Agent pursuant to these Instructions shall, until applied as herein provided, be held in trust for the purposes for which they were received and shall be segregated from other funds. PWCo and/or PSWID shall provide such documentation as may reasonably be requested by Escrow Agent to authorize the investment of funds held by Escrow Agent pursuant to these Instructions.

(d) No provision of these Instructions shall be construed to relieve Escrow Agent from liability for its own negligent action, its own negligent failure to act, or its own willful misconduct.

6. Resignation by Escrow Agent. Escrow Agent may at any time resign by giving at least thirty (30) days' written notice to the PWCo and PSWID. Escrow Agent's resignation shall become effective on the earlier of (i) the date stated in the resignation given pursuant to the preceding sentence; or (ii) the date on which a successor Escrow Agent appointed and accepts the duties of Escrow Agent. In case Escrow Agent shall resign pursuant to this section, or otherwise become incapable of acting hereunder, an independent successor shall be appointed jointly by PWCo and PSWID.

7. Requests of Accounting. Upon request by PWCo or PSWID, a copy of Escrow Agent's record of accounting for funds received and disbursed, on Escrow Agent's form, shall be furnished to the requesting party.

8. Notices.

(a) Any notice, approval, consent or other communication required or permitted to be given to a Party must be in writing and delivered in person, or by reputable nationwide overnight

courier (e.g., Federal Express), or given by facsimile transmission, or forwarded by certified or registered mail, postage pre-paid, return receipt requested, at the address indicated below, unless the Party giving such notice has been notified, in writing, of a change of address:

PWCo:

Brooke Utilities, Inc.
Attention: Robert T. Hardcastle, President
3101 State Road
Bakersfield, CA 93308
Telephone: (661) 633-7526
Facsimile: (800) 748-6981
email: rth@brookeutilities.com

With a copy to:

Jay L. Shapiro
Fennemore Craig, P.C.
3003 N. Central Avenue, Suite 2600
Phoenix, Arizona 85012
Telephone: (602) 916-5366
Facsimile: (602) 916-5566
Email: jshapiro@fclaw.com

PSWID:

Pine Strawberry Water Improvement District
Attention: Gary Sherlock, Chairman
P.O. Box 134 Pine, Arizona
H- 928-476-3560
C- 602-989-1942
rgse@earthlink.net

With a copy to:

William P. Sullivan, Esq.
Curtis, Goodwin, Sullivan, Udall & Schwab
501 East Thomas Road
Phoenix, AZ 85006-1003
Telephone: (602) 393-1700
Facsimile: (602) 393-1703
Email: wsullivan@cgsuslaw.com

Escrow Agent:

Pioneer Funding Services
Attention: Richard L. Gann
14500 N. Northsight Blvd., Suite 112
Scottsdale, AZ 85260
Telephone: (480) 607-7308, Ext. #205
Facsimile: (480) 607-7284 or (866) 530-8589
Email: Rich.Gann@PTAAZ.com

- (b) Notices shall be effective in accordance with the following:
- (i) On the earliest of date of delivery (or refusal to accept delivery) if notice is given by personal delivery or facsimile transmission with evidence of error-free transmission prior to 5:00 p.m., Arizona time;
 - (ii) On a business day (or the next succeeding business day if given after 5:00 p.m., Arizona time or on a Saturday, Sunday or federal or Arizona state holiday);
 - (iii) On the next succeeding business day after deposit with an overnight courier for next day delivery; or
 - (iv) If notice is sent through the United States mail, on the earlier of the date of actual delivery as shown by the addressee's receipt or the expiration of three (3) days following the date of mailing.

9. Miscellaneous Provisions.

(a) Attorneys' Fees. If any party is in default hereunder, the defaulting party shall pay for other party's reasonable attorneys' fees, expert witness fees, deposition and trial transcript costs and cost of court and other similar costs or fees paid or incurred by the other party by reason of or in connection with the default (whether or not legal or other proceedings are instituted).

(b) Entire Agreement. These Instructions constitutes the entire agreement between the parties hereto pertaining to the retention and disbursement of the PSWID Funds. No change or addition is to be made to these Instructions except by written amendment executed by the parties hereto.

(c) Successors and Assigns. These Instructions shall inure to the benefit of, and be binding upon, the parties hereto and their successors-in-interest and permitted assigns.

(d) No Third Party Beneficiary. These Instructions is intended solely for the benefit of PWCo and PSWID. No third party will have any rights or interest in any provision of these Instructions or the PSWID Funds.

(e) Waiver. No delay in exercising any right or remedy shall constitute a waiver thereof; and no waiver by the PSWID or PWCo of the breach of any covenant of these Instructions shall be construed as a waiver of any proceeding or succeeding breach of the same or any other covenant or condition of these Instructions.

(f) Severability. If any provision of these Instructions shall be determined by a court to be illegal, inoperative or unenforceable, the same shall not affect any other provision or provisions herein contained or render the same invalid, inoperative or unenforceable to any extent whatever.

(g) Multiple Counterparts. These Instructions may be executed in multiple counterparts, each of which shall be an original and all of which combined shall constitute one and the same instrument.

(h) Authorized Signatures. The individuals executing and acknowledging these Instructions on behalf of the respective parties are authorized to do so and, upon their execution and acknowledgement, these Instructions shall be binding and enforceable upon the respective parties in accordance with its terms and provisions.

[SIGNATURE PAGE FOLLOWS]

IN WITNESS WHEREOF, the Parties have executed these Instructions as of the date first set forth above.

PWCo:

PINE WATER COMPANY

By: _____
Name: _____
Title: _____

PSWID:

PINE-STRAWBERRY WATER
IMPROVEMENT DISTRICT

By: _____
Name: _____
Title: _____

ESCROW AGENT:

ACCEPTED AND AGREED TO:

PIONEER TITLE AGENCY, INC., an
Arizona corporation

By: _____
Name: _____
Title: _____

Exhibit "A"

Schedule of Escrow Fees

Pioneer Funding Services

Schedule of Escrow Fees and Expenses

A service fee in the amount of \$350.00 shall be due Escrow Agent upon the execution of this Escrow Instruction. This fee represents the total cost for the escrow services described herein including up to one disbursed check or wire. In the event additional disbursements are required by the parties, Escrow Agent shall be due an additional service fee in the amount of \$15.00 per each additional check or wire disbursed.