

OPEN MEETING ITEM



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ORIGINAL



COMMISSIONERS
MIKE GLEASON - Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

ARIZONA CORPORATION COMMISSION

DATE: FEBRUARY 22, 2008

DOCKET NO: W-02234A-07-0371

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Sarah Harpring. The recommendation has been filed in the form of an Opinion and Order on:

H2O, INC.
(CC&N EXTENSION)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

MARCH 3, 2008

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

MARCH 11, 2008 and MARCH 12, 2008

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602)542-4250. For information about the Open Meeting, contact the Executive Secretary's Office at (602) 542-3931.

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AZ CORP COMMISSION
DOCKET CONTROL

BRIAN C. McNEIL
EXECUTIVE DIRECTOR

Arizona Corporation Commission
DOCKETED

FEB 22 2008

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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 MIKE GLEASON, Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 KRISTIN K. MAYES
7 GARY PIERCE

8 IN THE MATTER OF THE APPLICATION OF
9 H2O, INC. FOR AN EXTENSION OF ITS
10 CERTIFICATE OF CONVENIENCE AND
11 NECESSITY TO PROVIDE WATER SERVICE IN
12 PINAL COUNTY, ARIZONA.

DOCKET NO. W-02234A-07-0371

DECISION NO. _____

13 OPINION AND ORDER

14 DATE OF HEARING: January 17, 2008
15 PLACE OF HEARING: Phoenix, Arizona
16 ADMINISTRATIVE LAW JUDGE: Sarah N. Harpring
17 APPEARANCES: Mr. Richard L. Sallquist, SALLQUIST, DRUMMOND
18 & O'CONNOR, P.C., on behalf of H2O, Inc.; and
19 Ms. Kenya Collins, Staff Attorney, Legal Division, on
20 behalf of the Utilities Division of the Arizona
21 Corporation Commission.

22 **BY THE COMMISSION:**

23 On June 15, 2007, H2O, Inc. ("H2O") filed with the Arizona Corporation Commission
24 ("Commission") an application to extend its Certificate of Convenience and Necessity ("CC&N") to
25 provide water utility service in portions of Pinal County, Arizona.

26 On July 13, 2007, the Commission's Utilities Division Staff ("Staff") issued an Insufficiency
27 Letter.

28 On September 24, 2007, H2O filed a Response to Staff's Insufficiency Letter.

On October 5, 2007, H2O filed, as a late-filed exhibit to its application, an Approval to
Construct ("ATC") issued by the Arizona Department of Environmental Quality ("ADEQ") for the
water line to serve the J.O. Combs Educational Village.

On October 24, 2007, Staff filed a Sufficiency Letter, indicating that H2O's application had
met the sufficiency requirements outlined in the Arizona Administrative Code ("A.A.C.").

On October 30, 2007, a Procedural Order was issued scheduling a hearing in this matter for

1 January 17, 2008, and establishing other procedural deadlines and requirements.

2 On November 30, 2007, a Staff Report was filed.

3 On December 18, 2007, H2O filed an Affidavit of Publication.

4 On January 17, 2008, a full public hearing was held before a duly authorized Administrative
5 Law Judge of the Commission at its offices in Phoenix, Arizona. H2O and Staff appeared through
6 counsel and presented evidence and testimony. No members of the public appeared to give public
7 comment. At the hearing, H2O was requested to file, by February 1, 2008, a late-filed exhibit
8 showing all of its wells and their current status in terms of operation and with ADEQ, including
9 arsenic test results. Staff was requested to provide a response to the late-filed exhibit within 10 days
10 after its receipt. At the close of the hearing, the matter was taken under advisement pending receipt
11 of the late-filed exhibit and Staff's response.

12 On January 31, 2008, H2O filed a late-filed exhibit regarding its wells and their status.

13 On February 7, 2008, Staff filed its response to H2O's late-filed exhibit.

14 On February 11, 2008, H2O filed a supplement to its late-filed exhibit, with copies of ADEQ
15 ATCs for several of its wells.

16 * * * * *

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

19 **FINDINGS OF FACT**

20 1. H2O is an Arizona public service corporation authorized to provide water utility
21 service in parts of Pinal and Maricopa Counties, Arizona, pursuant to authority granted by the
22 Commission. According to the Staff Report, H2O's current CC&N area is approximately 11,640
23 acres in size.

24 2. H2O incorporated in Arizona in October 1972 and is in good standing with the
25 Commission's Corporations Division. According to Staff, H2O has no outstanding Commission
26 compliance issues.

27 3. On June 15, 2007, H2O filed with the Commission an application to extend its CC&N
28 to provide water utility service by adding the western one-half of Section 9, Township 2 South,

1 Range 8 East of the Gila and Salt River Base and Meridian, Pinal County, Arizona ("CC&N
2 extension area").

3 4. The CC&N extension area is approximately 320 acres in size and is comprised of two
4 parcels, the school parcel, which is 108.151 acres in size, and the residential parcel, which is 211.85
5 acres in size. As shown in Exhibit A, attached hereto, the school parcel is situated in the northern and
6 midwest portion of the CC&N extension area, and the residential parcel comprises the remainder.
7 The entire CC&N extension area is Arizona state trust land administered by the Arizona State Land
8 Department ("ASLD").

9 5. H2O had notice of its application and the January 17, 2008, hearing date published in
10 the *Florence Reminder and Blade-Tribune* on November 22, 2007, within the deadline established by
11 the Procedural Order issued on October 30, 2007.

12 6. The CC&N extension area is included within H2O's Pinal County Franchise, which
13 was renewed for a period of 25 years by the Pinal County Board of Supervisors on February 17,
14 1999.

15 7. According to Staff, H2O's annual report for calendar year 2006 shows a net profit of
16 \$26,406.53, and H2O reported \$207,958.03 in outstanding long-term debt.

17 8. According to the Staff Report, H2O has an approved curtailment tariff for its system.

18 9. Mr. Donald Schnepf, President of H2O, testified that, in the CC&N extension area,
19 H2O intends to use only those rates and charges authorized by the Commission and will provide
20 service in a manner similar to that in which it is providing service to its other service areas and in
21 accordance with the Commission's rules and regulations. (Tr. at 53, lines 16-23.)

22 10. At hearing, Staff was uncertain who was to provide sewer service for the CC&N
23 extension area. (Tr. at 20, lines 9-16) H2O's counsel asserted that Johnson Utilities has a pending
24 wastewater CC&N application before the Commission for the CC&N extension area. According to
25 the Commission's e-Docket, in August 2007, in Docket No. WS-02987A-07-0487, Johnson Utilities
26 filed an application for extension of its wastewater CC&N to include the entire CC&N extension
27 area, among other land, and specifically stated therein that its application was made at the request of
28 the J.O. Combs School District.

1 11. With its application, H2O included a letter dated July 31, 2006, requesting H2O to
2 provide water service for the J.O. Combs Academic Campus, described as including an elementary
3 school, middle school, and high school. In the letter, the developer is identified as the J.O. Combs
4 School District #44.

5 12. In its application, H2O asserted that the ASLD could not provide a request for service
6 at that time due to ASLD policies. However, H2O subsequently provided a letter from the ASLD,
7 dated September 12, 2007, stating in regard to H2O's application for the CC&N extension area that
8 the ASLD has issued a long term lease to J.O. Combs Unified School District and that it is in the best
9 interest of state trust land to be included in this certificated area for water delivery. At hearing, both
10 H2O and Staff testified to their understanding that the ASLD letter covers the entire CC&N extension
11 area, all of which is state trust land. (Tr. at 28, lines 23-25; Tr. at 29, lines 1-25; Tr. at 30, lines 1-21;
12 Tr. at 35, lines 5-8.)

13 13. H2O's water system currently has four active wells with a combined production
14 capacity of 4,950 gallons per minute ("GPM"), eight storage tanks with a combined storage capacity
15 of approximately 5.2 million gallons,¹ and a distribution system that is serving approximately 8,000
16 service connections.² Based on historical growth rates, Staff anticipates that the existing service area
17 could grow to approximately 13,200 service connections at the end of five years. H2O has predicted
18 an additional 268 connections for the CC&N extension area at the end of five years, resulting in a
19 projected total customer base of approximately 13,500 at the end of five years. Based on well
20 production and storage capacities, Staff estimates that the existing system can serve approximately
21 9,550 service connections. Staff stated that H2O is also constructing three additional wells with a
22 combined production capacity of 4,500 GPM, which will result in the system's ability to serve more
23
24

25 _____
26 ¹ The Staff Report and Staff's response to H2O's late-filed exhibit stated that H2O's eight storage tanks have a
27 combined capacity of 4.9 million gallons. However, at hearing, H2O stated that there are 10 storage tanks in use with a
28 combined capacity of 6,965,000 gallons, (Tr. at 47, lines 4-5), and H2O's late-filed exhibit shows that there are 8 storage
tanks in use, with a capacity of approximately 5.2 million gallons, and another 2 storage tanks that have been completed
but are not yet in use, with a capacity of approximately 1.7 million gallons.

² The Staff Report stated that H2O was providing service to 6,668 service connections as of December 31, 2006. H2O
testified that it is currently serving approximately 8,000 service connections. (Tr. at 33, lines 2-4.)

1 than 18,000 service connections.³

2 14. Staff has determined that H2O's existing water system has adequate production and
3 storage capacity to serve the existing CC&N area and can reasonably be expected to develop
4 additional production and infrastructure as required within a conventional five-year period.

5 15. According to the Staff Report, H2O estimated that it will need to add approximately
6 36,283 feet of piping to serve both parcels of the CC&N extension area, at a cost of approximately
7 \$897,241, which will be financed using advances in aid of construction pursuant to main extension
8 agreements between H2O and developers. Mr. Schnepf testified that the School District will build
9 and own its own on-site facilities for the schools, but that the infrastructure for the residential parcel
10 will be funded through standard hook-up fees and line extension agreements. (Tr. at 46, lines 4-10.)

11 16. Mr. Schnepf testified that the J.O. Combs School District is already constructing a
12 grade school, which is scheduled to open later this year; has a high school under construction that is
13 scheduled to open in 2009; and intends to construct a middle school that is scheduled to open in 2010.
14 (Tr. at 34, lines 12-25.)

15 17. Mr. Schnepf testified that development of the residential parcel will begin some time
16 in the future after the ASLD sells the residential parcel, which will be surrounded on all four sides by
17 H2O's CC&N, to a developer. (Tr. at 37, lines 21-24.) Mr. Schnepf testified that he believes this
18 land will be developed for residential use because it would be very difficult to use for agricultural
19 activities due to restrictions on the use of pesticides and other agricultural chemicals within close
20 proximity to schools. (Tr. at 37, line 25; Tr. at 38, lines 1-4.)

21 **Compliance with Arizona Department of Water Resources ("ADWR") Requirements**

22 18. According to Staff, the CC&N extension area is located within the Pinal Active
23 Management Area ("AMA"), as designated by ADWR, and ADWR has indicated to Staff that H2O is
24 in compliance with the Pinal AMA reporting and conservation requirements.

25 19. Staff has recommended that H2O be required to file with Docket Control, as a
26 compliance item in this docket, within two years after the effective date of this Order, copies of a

27 ³ According to H2O's late-filed exhibit regarding its wells and system, H2O actually has four additional wells that will
28 soon be ready for use, three of which will be ready for test pumping in February 2008 and one for which the ADEQ
Approval of Construction is expected in March 2008. The four wells have a capacity of 6,000 GPM.

1 Certificate of Assured Water Supply ("CAWS") issued by ADWR for the residential parcel. Staff
2 has further recommended that H2O's CC&N extension be considered null and void after due process
3 should H2O fail to make this filing within the time specified.

4 **Compliance with ADEQ Requirements**

5 20. According to Staff, ADEQ determined in September 2007 that H2O's public water
6 system has no deficiencies, and ADEQ has determined that the system is currently delivering water
7 that meets the water quality standard requirements of 18 A.A.C. 4.

8 21. On October 5, 2007, H2O filed with Docket Control a copy of its ATC for 15,100
9 linear feet of 12-inch water line to serve the J.O. Combs Educational Village in Queen Creek, Pinal
10 County (the school parcel).

11 22. Staff recommended that H2O be required to file with Docket Control, as a compliance
12 item in this docket, within two years after the effective date of this Order, copies of the ATC for the
13 facilities needed to serve the residential area. Staff has further recommended that H2O's CC&N
14 extension be considered null and void after due process should H2O fail to make this filing within the
15 time specified.

16 **H2O's Ability to Comply with Staff's Recommended Filing Deadlines**

17 23. Mr. Schnepf testified that Staff's recommended two-year deadline to file an ATC for
18 the water facilities in the residential parcel and a CAWS for the residential parcel may be insufficient
19 for reasons outside of H2O's control. (Tr. at 47, lines 12-20.) Specifically, Mr. Schnepf testified that
20 no one knows when development will occur in the residential parcel because of the state of the
21 current economy and because it will depend on when the ASLD decides to sell the residential parcel.
22 (Tr. at 47, lines 21-23.) Mr. Schnepf also stated that it is the developer who must obtain the CAWS
23 from ADWR. (Tr. at 48, lines 4-17.)

24 24. Mr. Schnepf testified that H2O would prefer to have an open-ended requirement to file
25 the CAWS and ATC when received, as H2O has received in another Commission Decision.⁴ (Tr. at

26 ⁴ In Decision No. 69966 (October 30, 2007), the Commission granted H2O final approval of a CC&N extension
27 although H2O had not yet been able to file CAWS and ATCs within two years as required in Decision No. 63960
28 (September 4, 2001), as amended by Decision No. 64062 (October 4, 2001). H2O had received a two-year extension by
Procedural Order on October 30, 2003 (making the filing deadline four years after the Order), and Staff had determined
that H2O's inability to meet the compliance dates was related solely to the problems of the developers and that granting

1 51, lines 13-21.)

2 25. When asked by Counsel for H2O whether she had an objection to modifying her
3 recommendations that H2O file the CAWS and ATC for the residential parcel within two years after
4 the effective date of this Order, Ms. Blessing Chukwu, Executive Consultant III for the Commission,
5 testified that she would not support leaving the filing deadline open-ended because it would be very
6 difficult to track for compliance purposes. (Tr. at 13, lines 6-8.) Ms. Chukwu further testified that if
7 she had been aware of H2O's objection to the two-year deadline, she would have recommended an
8 order preliminary for the residential parcel due to the uncertainty of when the residential parcel will
9 be developed. (Tr. at 14, lines 15-20.) Ms. Chukwu testified that if the deadline is more than two
10 years, she would recommend an order preliminary, (Tr. at 15, lines 24-25), but also stated that with a
11 two-year deadline, H2O could always file for an extension, (Tr. at 16, lines 1-5). Ms. Chukwu
12 testified that with an order preliminary for state trust land, she would recommend a five-year deadline
13 for the filing requirements. (Tr. at 24, lines 12-15.)

14 26. Ms. Chukwu also testified that it will probably be more economical, for economies of
15 scale reasons, to give the residential parcel to H2O because it is unlikely that anyone else is going to
16 desire to provide service in that area, which is surrounded by H2O's existing CC&N area and the
17 school parcel. (Tr. at 25, lines 1-15.) Further, Ms. Chukwu stated that she is even more inclined to
18 recommend granting the residential parcel to H2O because it is state trust land. (Tr. at 25, lines 16-
19 20.) Ms. Chukwu ultimately testified that her recommendation for the residential parcel is the two-
20 year deadline included in the Staff Report, because one school is already being constructed, a total of
21 three schools will be constructed, and Ms. Chukwu believes that houses tend to go up pretty quickly
22 around schools. (Tr. at 26, lines 11-22; Tr. at 27, lines 1-4.)

23 27. Although we agree with Staff that an open-ended filing requirement would be difficult
24 to track for compliance purposes, we also recognize the validity of H2O's concerns regarding the
25 ability to obtain the CAWS and ATC for the residential parcel within two years after the effective
26 date of this Order, especially in light of the current state of the economy in general and the housing

27 an additional extension request would not be productive. Staff instead recommended that final approval of the CC&N
28 extension be approved. In Decision No. 69966, the Commission ordered that the outstanding compliance requirements of
Decision No. 64062 remain in effect and that H2O file the required documentation when received.

1 market in particular. We also share Staff's belief that it is very unlikely that another public service
2 corporation would desire to provide water utility service to the residential area, which is only 211.85
3 acres in size and, after the granting of a CC&N extension to H2O for the school parcel, will be
4 completely surrounded by H2O's CC&N area. We also agree with Staff that the proximity of the
5 residential parcel to a new school complex increases the likelihood that it will be developed for
6 housing within the next few years. In light of these factors, we believe that it is appropriate to modify
7 Staff's recommendations to allow H2O three years from the effective date of this Order to file with
8 Docket Control the CAWS and ATC for the residential parcel, with the ability to seek an extension if
9 necessary.

10 **Arsenic Levels**

11 28. The U.S. Environmental Protection Agency ("EPA") has reduced the maximum
12 contaminant level ("MCL") for arsenic in drinking water to 10 parts per billion ("ppb"). Mr. Schnepf
13 testified that none of the wells in H2O's system have had any difficulty with arsenic levels. (Tr. at
14 52, lines 5-7.) H2O provided arsenic test results for all four of its active wells and two of its new
15 wells, all of which ranged between <2 ppb and 3 ppb, well below the EPA's MCL for arsenic.

16 **Groundwater Use within the CC&N Extension Area**

17 29. Mr. Schnepf testified that the only turf-related facilities in the CC&N extension area
18 of which he is aware would be a playground area and a ball field. (Tr. at 44, lines 14-18.) He is not
19 aware of any water amenities, lakes, ponds, golf courses, or even water fountains that are being
20 planned for any part of the CC&N extension area. (Tr. at 44, lines 18-22.)

21 **Compliance with Arizona Department of Revenue Requirements**

22 30. Mr. Schnepf testified that H2O is current on its property and sales taxes with the
23 Arizona Department of Revenue. (Tr. at 52, lines 21-23.)

24 **Staff's Recommendations**

25 31. Staff has recommended that H2O be required to charge its authorized rates and
26 charges in the CC&N extension area.

27 32. Ms. Chukwu testified that H2O is capable, fit, and proper to provide service to the
28 CC&N extension area, (Tr. at 9, lines 1-4), and that granting H2O a CC&N would serve the public

1 interest, (Tr. at 9, lines 12-14).

2 33. Staff has recommended that H2O's application for a CC&N extension as to the CC&N
3 extension area be approved, subject to the conditions described in Finding of Fact Nos. 19, 22, and
4 31.

5 **Other Recommendations**

6 34. Because an allowance for property tax expense is included in H2O's rates and will be
7 collected from its customers, the Commission seeks assurances from H2O that any taxes collected
8 from ratepayers have been remitted to the appropriate taxing authority. It has come to the
9 Commission's attention that a number of water companies have been unwilling or unable to fulfill
10 their obligation to pay the taxes that were collected from ratepayers, some for as many as 20 years. It
11 is reasonable, therefore, that as a preventive measure H2O shall annually file, as part of its annual
12 report, an affidavit with the Utilities Division attesting that H2O is current in paying its property
13 taxes in Arizona.

14 35. In recent months, the Commission has become increasingly concerned about the
15 prolonged drought in Central Arizona. Therefore, we believe H2O should be required to conserve
16 groundwater and that H2O should be prohibited from selling groundwater for the purpose of
17 irrigating any future golf courses within the certificated expansion area or any ornamental lakes or
18 water features located in the common areas of the proposed new development within the certificated
19 expansion areas.

20 **CONCLUSIONS OF LAW**

21 1. H2O is a public service corporation within the meaning of Article XV of the Arizona
22 Constitution and A.R.S. § 40-281 *et seq.*

23 2. The Commission has jurisdiction over H2O and the subject matter of the application.

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

25 4. There is a public need and necessity for water utility services in the requested CC&N
26 extension area described and shown in Exhibit A, attached hereto and incorporated herein.

27 5. H2O is a fit and proper entity to receive an extension of its CC&N for water utility
28 services to include the CC&N extension area described and shown in Exhibit A.

1 IT IS FURTHER ORDERED that, in light of the ongoing drought conditions in Central
2 Arizona and the need to conserve groundwater, H2O, Inc. is prohibited from selling groundwater for
3 the purpose of irrigating any future golf courses within the certificated expansion area or any
4 ornamental lakes or water features located in the common areas of the proposed new development
5 within the certificated expansion area.

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

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.
8
9

10 CHAIRMAN _____ COMMISSIONER _____

11
12 COMMISSIONER _____ COMMISSIONER _____ COMMISSIONER _____

13
14 IN WITNESS WHEREOF, I, DEAN S. MILLER, Interim
15 Executive Director of the Arizona Corporation Commission,
16 have hereunto set my hand and caused the official seal of the
17 Commission to be affixed at the Capitol, in the City of Phoenix,
18 this ____ day of _____, 2008.

19 _____
20 DEAN S. MILLER
21 INTERIM EXECUTIVE DIRECTOR

22 DISSENT _____

23 DISSENT _____

24 SNH:db

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SERVICE LIST FOR: H2O, INC.

DOCKET NO.: W-02234A-07-0371

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Utilities Division
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, AZ 85007

EXHIBIT A

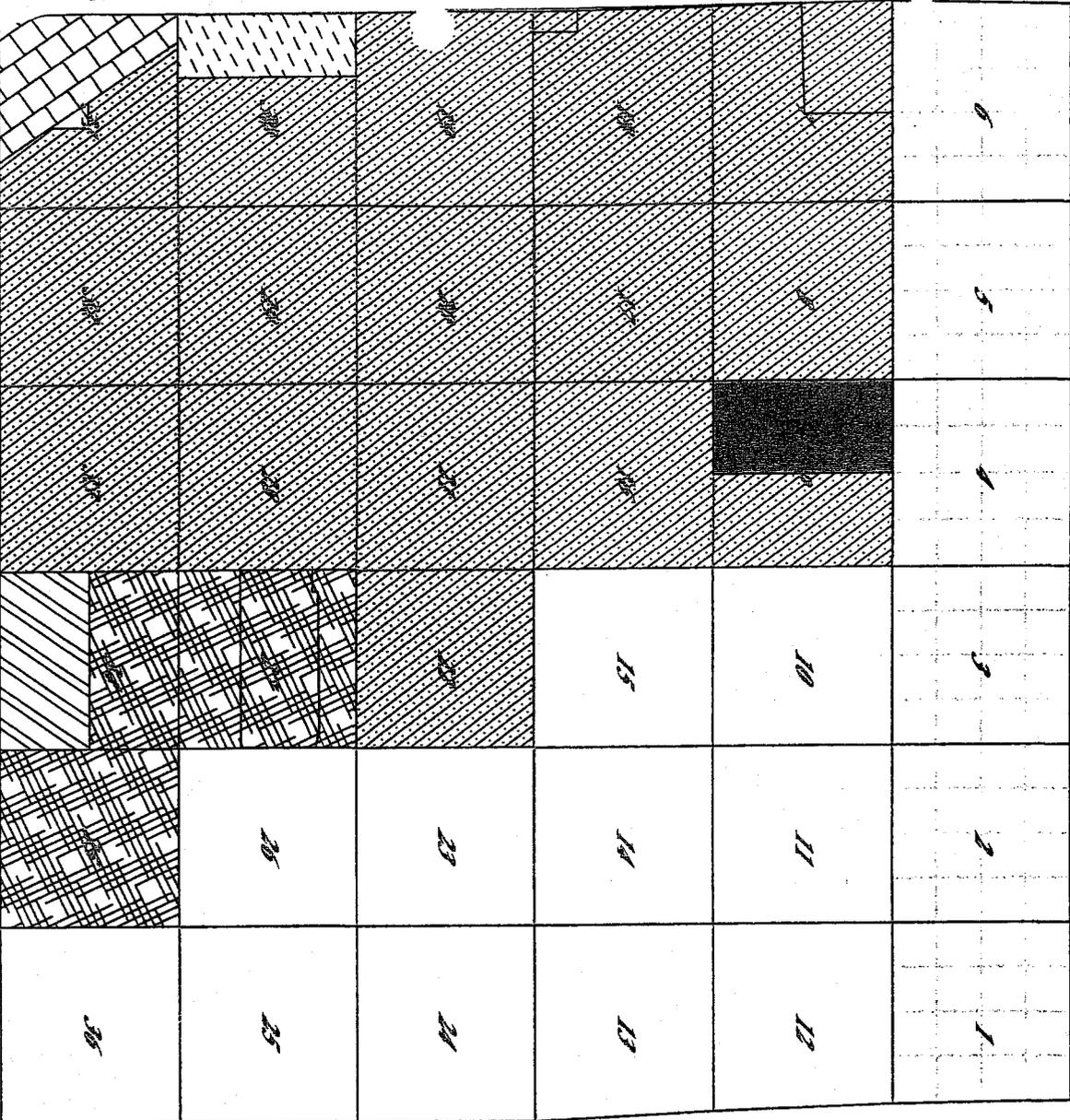
LEGAL DESCRIPTION

The West one-half of Section 9, Township 2 South, Range 8 East of the G&SRB&M, Pinal County, Arizona.

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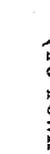
COUNTY OF Pinal

RANGE 8 East



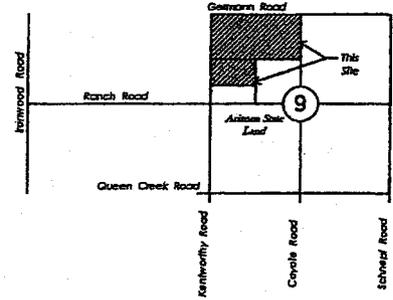
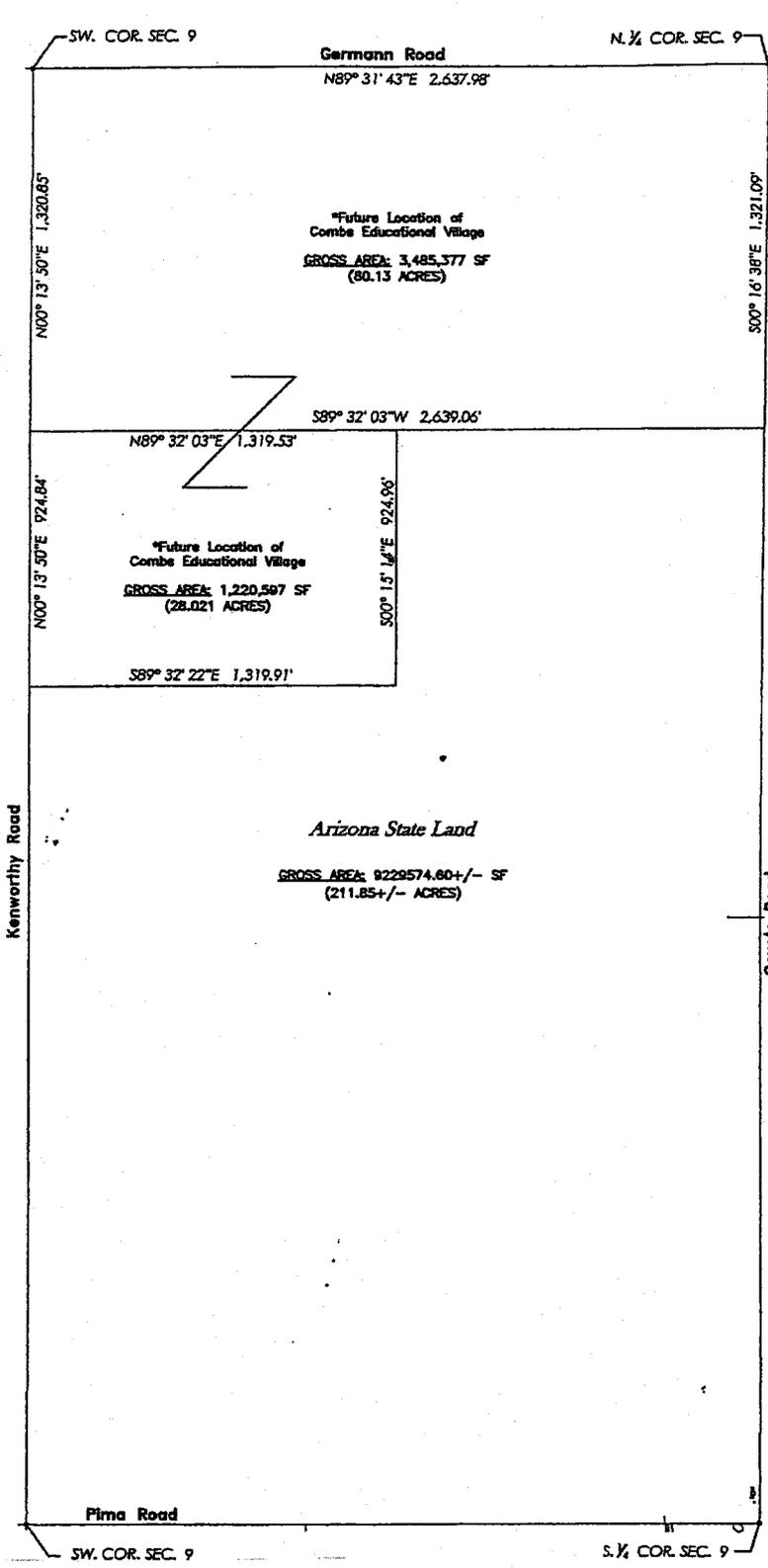
TOWNSHIP 2 South

DECISION NO. _____

-  WS-2987 (6)
-  Sewer
-  Johnson Utilities Company
-  W-2859 (3)
-  Diversified Water Utilities, Inc.
-  W-2234 (2)
-  H₂O, Inc.
-  W-1395 (2)
-  Queen Creek Water Company
-  W-2425 (2)
-  Sun Valley Farms Unit VI Water Company
-  W-2425 (2)
-  (1)
-  H₂O, Inc.
-  Docket No. W-02234A-07-0371
-  Application for Extension
-  Johnson Utilities, LLC
-  Docket No. WS-02987A-07-0203
-  Application to Cancel Water & Sewer CC&NS
-  (To Town of Florence)

ATTACHMENT 1

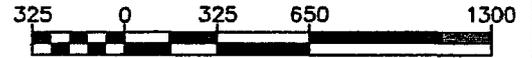
W¹/₂ Sec. 9 T2S R8E G. & S.R.M.



Vicinity Map
N.T.S.



GRAPHIC SCALE



(IN FEET)
1 INCH = 650 FT

H2O Inc.

DOMESTIC SERVICES

WATER UTILITY QUEEN CREEK, AZ

41502 N. Schreyer Rd.
Queen Creek, AZ 85240

Ph: (480) 491-6971
Fax: (480) 491-6739

DECISION NO. _____