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BEFORE THE ARIZONA CORPORATION COMMISSION

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JIM IRVIN
COMMISSIONER
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COMMISSIONER

Arizona Corporation Commission

DOCKETED

MAR 28 2002

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ARIZONA CORPORATION COMMISSION
DOCUMENT CONTROL

DOCKETED BY

IN THE MATTER OF THE APPLICATION OF
THE ARIZONA ELECTRIC DIVISION OF
CITIZENS COMMUNICATIONS COMPANY TO
CHANGE THE CURRENT PURCHASED
POWER AND FUEL ADJUSTMENT CLAUSE
RATE, TO ESTABLISH A NEW PURCHASED
POWER AND FUEL ADJUSTMENT CLAUSE
BANK, AND TO REQUEST APPROVED
GUIDELINES FOR THE RECOVERY OF COSTS
INCURRED IN CONNECTION WITH ENERGY
RISK MANAGEMENT INITIATIVES.

Docket No. E-01032C-00-0751

**MOHAVE COUNTY AND SANTA
CRUZ COUNTY'S BRIEF ON ISSUES
RAISED BY THE MOTION TO
RECUSE**

Intervenors Mohave County and Santa Cruz County (collectively, the "Counties"), through undersigned counsel, hereby respectfully submit their Brief on various issues raised in connection with the "Motion for the Law Firm "Gallagher & Kennedy" to Recuse Due to a Possible Conflict of Interest in Docket E-01032C-00-0751" (the "Motion to Recuse"), as follows:

1. INTRODUCTION.

The Motion to Recuse would have the law firm of Gallagher & Kennedy ("G&K") voluntarily withdraw or otherwise be disqualified from representing Citizens in this proceeding. The basis for the Motion to Recuse is that G&K has a conflict of interest. Subsequently, the Commission has indicated that the public interest might also require that the Motion to Recuse be granted based upon the appearance of a conflict of interest.

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The Motion for Recuse argues that G&K’s conflict of interest arises because (1) Citizens and APS are adverse parties to power sale agreements that are the subject of the Commission’s inquiry in this proceeding; and (2) Michael Gallagher, a founding member and shareholder of G&K, is a member of the Board of Directors of Pinnacle West Capital Corporation (“PinWest”) and Arizona Public Service Corporation (“APS”) ¹. G&K also acknowledges that it simultaneously represents Citizens, PinWest and APS in other matters.

Citizens does not deny that G&K has a conflict of interest. Instead, Citizens in response to the Motion to Recuse, has submitted Affidavits of Mr. Gallagher, Mr. Michael Kennedy and representatives of PinWest and APS to demonstrate that G&K took all of the steps required by the Rules of the Arizona Supreme Court to obtain a waiver of the conflict of interest. Thus, Citizens argues that “there is not even the appearance of impropriety and recusal is simply not warranted”. See Supplement to Citizens’ Opposition, etc., at 4. Citizens also argues that the Commission lacks the authority to grant the Motion to Recuse.

The Commission has asked the parties to address several unresolved issues raised in connection with the Motion to Recuse. The Counties characterize these issues as follows: (1) Can APS, Pinwest and Citizens waive G&K’s conflict of interest? (2) Are there public interest considerations that would justify granting the Motion to Recuse for the “appearance of impropriety”?; and (3) Does the Commission have the authority to grant the Motion to Recuse?

¹ PinWest and APS shall sometimes be collectively referred to as “APS”.

1 **2. RESPONSE TO CITIZENS' OPPOSITION TO THE MAGRUDER**
2 **MOTION TO RECUSE.**

3
4 Arizona Rules of the Supreme Court, Rule 42, ER 1.7 ("ER 1.7") provides that a
5 lawyer shall not represent a client if the representation will be directly adverse to another
6 client or if conflicting interests materially limit the representation unless (1) the
7 representation will not adversely affect the relationship with the other client and (2) each
8 client consents after consultation.

9
10 It appears that G&K does have a conflict of interest. G&K represents both Citizens
11 and APS at a time when they are adverse parties to (1) the 2001 Power Sale Agreement at
12 issue in this case; (2) the audit of the 1995 Power Sale Agreement; (3) unresolved disputes
13 regarding overcharges pursuant to the 1995 Power Sale Agreement; and (4) other claims
14 that have been identified by Citizens' attorneys related to the 1995 Power Sale Agreement.
15 Moreover, Michael Gallagher, a shareholder in G&K is a member of the Board of
16 Directors of PinWest and APS.

17
18 However, the Comments to ER 1.7 state that "A client may consent to
19 representation notwithstanding a conflict" and "Resolving questions of conflict of interest
20 is primarily the responsibility of the lawyer undertaking the representation".

21
22 The documents submitted in response to the Motion to Recuse establish that G&K
23 consulted with Citizens, APS and PinWest regarding the conflict of interest. Citizens,
24 APS and PinWest waived the G&K conflict of interest in writing. See Michael Kennedy
25 Affidavit at para. 9. Although it appears that Mr. Gallagher attended PinWest and APS
26 Board meetings at which Citizens' issues were discussed, G&K has isolated Mr. Gallagher

1 from the law firm's representation of Citizens. See Michael Kennedy Affidavit at para. 6.

2 In this instance G&K took the steps required by ER 1.7 to obtain waivers of the
3 conflict of interest from Citizens, APS and PinWest. Each G&K client appears to have
4 made a knowing waiver of the conflict of interest. G&K has acknowledged and addressed
5 Mr. Gallagher's dual role in accordance with accepted procedures. There does not seem
6 to be anything improper with the waiver or the manner in which it was obtained.
7

8 However, as discussed below, the prudence of Citizens' waiver is an issue that the
9 Commission should resolve in connection with its adjudication of this case.
10

11 **3. THE COUNTIES' RESPONSE TO THE COMMISSION'S**
12 **ADDITIONAL ISSUES.**

13 **A. Can G&K's conflict of interest be waived by APS, PinWest and**
14 **Citizens?**
15

16 ER 1.7 explicitly provides that under specified circumstances parties may waive their
17 attorney's conflict of interest. However, the law in Arizona also addresses situations where, for
18 public interest reasons, some conflicts may not be waived by the client due to their impact on
19 the public perception of the legal system. Comments to ER 1.7 state:
20

21 A client may consent to representation notwithstanding a conflict. However, as
22 indicated in paragraph (a) (1) with respect to representation directly adverse to
23 a client, and paragraph (b) (1) with respect to material limitations on
24 representation of a client, when a disinterested lawyer would conclude that the
25 client should not agree to the representation under the circumstances, the
26 lawyer involved cannot properly ask for such agreement or provide
representation on the basis of the client's consent.²

² ER 1.7 (b) addresses conflicts of interest where a lawyer's representation of a client may be materially limited by a lawyer's responsibility to another client, a third person or the lawyer's own interests.

1 This comment apparently has its roots in the former Canon 9 of the American Bar
2 Association's Code of Professional Responsibility. Former Canon 9 required that "a lawyer
3 should avoid even the appearance of professional impropriety." Under former Canon 9 a
4 lawyer could be disqualified if a court found (1) some specifically identifiable appearance of
5 improper conduct and (2) that "the likelihood of public suspicion or obloquy outweighs the
6 social interest which will be served by a lawyer's continued participation in a particular case."
7 See Woods v. Covington County Bank, 537 F.2d 804, 813 (5th Cir. 1976).
8
9

10 Former Canon 9 was deleted from the ABA Model Rules of Professional Conduct,
11 which have been adopted by Arizona. However, case law still suggests that there is some
12 continuing application of the "appearance of impropriety" rationale of former Canon 9. For
13 example, in Gomez v. Superior Court, 149 Ariz. 223, 717 P.2d 902 (1986), the Arizona
14 Supreme Court states:
15

16 It would appear, however, that 'appearance of impropriety', however weakened
17 by case law and its omission in the new Rules of Professional Conduct,
18 survives as a part of conflict of interest and an appearance of impropriety
19 should be enough to cause an attorney to closely scrutinize his conduct. It does
20 not necessarily follow that it must disqualify him in every case.

21 Id. at 225.

22 The Arizona Supreme Court added that in approaching "appearance of impropriety"
23 situations it strives for a "commonsense solution to this problem which protects the public and
24 yet makes available to public bodies the active participation of attorney members." Id. at 226.
25 The Court then articulated four factors that should be considered when ruling on a motion for
26 disqualification based upon the "appearance of impropriety":

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(1) whether the motion is being made for the purposes of harassing the [client], (2) whether the party bringing the motion will be damaged in some way if the motion is not granted, (3) whether there are any alternative solutions, or is the proposed solution the least damaging possible under the circumstances, and (4) whether the possibility of public suspicion will outweigh any benefits that might accrue due to continued representation.

Id.at 226 (quoting Alexander v. Superior Court, 141 Ariz. at 165).

The Counties believe that the Arizona Supreme Court’s analysis is designed to review each circumstance on its own merits and encourages the Commission to take strive for a “commonsense solution” in this case.

B. Are there public interest considerations in this case that would justify granting the Motion to Recuse for the “appearance of impropriety”?

Each circumstance of alleged “conflict of interest” or “appearance of impropriety” should be resolved based upon its own unique facts. In this instance, the Counties believe that there are two separate issues raised by the Motion to Recuse. Each issue merits its own analysis and conclusion.

The first issue deals with G&K’s conflict of interest. The determination of whether a conflict of interest exists and how to resolve matters of representation when a conflict of interest arises are matters within the jurisdiction of the judiciary and should be resolved in accordance with the legal and ethical standards adopted by the Arizona Supreme Court. The Counties believe that the Commission lacks authority to set standards for the determination and resolution of actual conflicts of interest between attorneys and clients that are different than those set by the Arizona Supreme Court. Williams v. Pipe Trades

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Industry Program of Arizona, 100 Ariz. 14, 19, 409 P.2d 720 (1966); Trico Electric Cooperative v. Ralston, 67 Ariz. 358, 359, 196 P.2d 470 (1948).

Based upon the information that has been provided, it appears that G&K properly followed the requirements of the Rules of the Arizona Supreme Court to obtain a valid waiver of conflict of interest. The record in this proceeding now contains Affidavits and legal briefs to support G&K's actions. Thus, there would not appear to be any impropriety on G&K's part in obtaining a waiver of conflict of interest to represent Citizens in this matter.

The second issue deals with whether Citizens' waiver of G&K's conflict of interest presents an "appearance of impropriety" that would undermine the integrity of the administrative proceeding currently pending before the Commission. The Counties recognize the vital importance of safeguarding the public confidence in the Commission's regulatory oversight of public service corporations. In this case, the Counties believe that the Commission has adequately protected the integrity of the proceeding by thoroughly investigating the claims in the Motion to Recuse. As a result of the Commission's additional inquiry into the relationship among G&K, Citizens, APS and PinWest, the record in this case now contains Affidavits, excerpts of Board Minutes and legal briefs addressing G&K's conflict of interest and the waiver thereof. The Counties believe that the Commission's actions have served to strengthen the public's confidence in this proceeding rather than allow unresolved questions as to the relationship between G&K and its clients linger.

1 The Counties do distinguish the public's confidence in the Commission from the
2 public's perception of Citizens. Indeed, the Counties believe that there is ample evidence
3 in the record of this case for the public to question the propriety of Citizens' decisions
4 regarding the Power Sale Agreements and its pursuit (or lack thereof) of APS for the
5 overcharged amounts.
6

7 However, any appearance of impropriety on the part of Citizens should be
8 considered when the Commission resolves this case. Indeed, the Counties believe that the
9 most appropriate way to ensure public confidence in this proceeding is to hold Citizens
10 accountable for its actions.
11

12 **C. Does the Commission have the authority to grant the Motion to Recuse?**

13 Although the Commission does not have the authority to supplant or re-define the Rules
14 of the Arizona Supreme Court, it does regulate the conduct of attorneys that are practicing
15 before it. A.A.C. R14-3-104 addresses the conduct required of persons appearing before the
16 Commission.
17

18 A.A.C. R14-3-104.E. provides that the Commission or presiding officer may permit the
19 withdrawal of an attorney from any proceeding. A.A.C. R14-3-104.F provides that persons
20 appearing before the Commission shall conform to the conduct expected in the Superior Court
21 of the State of Arizona. That section also states that (1) any alleged inappropriate conduct
22 before a Commissioner or a Hearing Officer shall be referred to the Commission for
23 appropriate action; (2) contemptuous conduct by any person appearing at a hearing shall be
24 grounds for his exclusion by the presiding officer from the hearing; and (3) if the Commission
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1 finds that any person has committed any improper or contemptuous conduct in any hearing
2 before the Commission or a presiding officer, the Commission may impose such penalties
3 provided by law that it deems appropriate. Thus, under the Commission's rules, it could grant
4 the Motion to Recuse if it determined that G&K engaged in inappropriate, improper or
5 contemptuous conduct and that disqualification was the appropriate remedy under the law.
6

7 **4. THE G&K CONFLICT ISSUE DOES IMPACT THE ANALYSIS OF**
8 **CITIZENS' PRUDENCE.**
9

10 The Counties believe that an appropriate alternative to granting the Motion to
11 Recuse is for the Commission to regard Citizens' waiver of the G&K conflict of interest
12 as a part of its overall analysis of the conduct by Citizens in its dealings with APS. This
13 Commission should factor into its deliberations the prudence of Citizens' waiver of the
14 G&K conflict of interest when it knew or should have known that the Power Sale
15 Agreements and overcharge dispute with APS would be material issues in this case.
16

17 Citizens believes that from May 2000 to May 2001, APS overcharged it by tens of
18 millions of dollars in purchase power costs under the 1995 Power Sale Agreement. In
19 fact, Citizens undertook an audit in connection with the overcharges. However, when
20 Citizens approached APS for information needed to complete the audit, APS refused to
21 cooperate. Citizens did not seek assistance from the Arizona Corporation Commission
22 ("Commission"), Federal Energy Regulatory Commission ("FERC") or the courts to
23 compel APS to produce the requested information. Instead, Citizens terminated its audit.
24
25 Citizens knew or should have known that as a result of filing its application in this case it
26

1 would require ongoing advice from legal counsel as to how it should pursue the
2 information from APS.

3
4 Citizens obtained a legal opinion, from counsel other than G&K, indicating that it
5 had a valid claim against APS for, among other things, breach of contract. When Citizens
6 threatened to take legal action against APS for recovery of the overcharges, APS stated
7 that it would vigorously defend itself. Citizens did not file any regulatory or legal action
8 to resolve the overcharge issue. Instead, Citizens negotiated a new agreement with higher
9 prices for purchase power. Citizens knew or should have known that as a result of filing
10 its application in this case it would require ongoing advice from legal counsel as to how it
11 should pursue the overcharge dispute with APS.
12

13
14 Citizens entered into the 2001 Power Sale Agreement with APS for a seven (7)
15 year term at a rate that is higher than those charged in the 1995 Power Sale Agreement.
16 Citizens knew or should have known that as a result of filing its application in this case it
17 would require ongoing advice from legal counsel as to the prudence of entering into the
18 2001 Power Sale Agreement.
19

20 The Counties believe that Citizens must answer legitimate questions regarding its
21 failure to pursue its remedies against APS in connection with the Phase III audit and
22 purchase power overcharges as well as entering into the 2001 Power Sale Agreement.
23 Whether it was prudent to waive G&K's conflict of interest is a relevant aspect of the
24 Commission's inquiry.
25

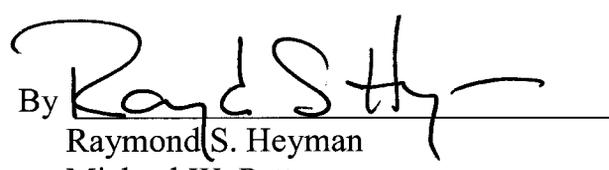
26 The Counties do believe that Citizens, G&K and the Commission have acted

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expeditiously in addressing the issues raised by the Motion to Recuse. The Counties believe that it is important that this issue be resolved in a manner that will satisfy all parties that a complete record will be provided to the Commission for a determination on the merits of this case.

RESPECTFULLY SUBMITTED March 28, 2002.

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