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Arizona Corporation Commission
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FENNEMORE CRAIG, P.C.
Jay L. Shapiro (No. 014650)
Todd C. Wiley (No. 015358)
3003 N. Central Ave.
Suite 2600
Phoenix, Arizona 85012

Attorneys for Pine Water Company, Inc.

BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF PINE WATER COMPANY FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE AND FOR APPROVAL TO INCUR LONG-TERM DEBT	DOCKET NO: W-03512A-03-0279 **PINE WATER COMPANY'S REPLY IN SUPPORT OF REQUEST FOR STAY** **Emergency Relief Requested**

Pine Water Company ("PWCo") submits this reply in support of its Request for Stay filed on May 15, 2009. In this reply, PWCo provides an update on the status of the condemnation proceedings filed by the Pine-Strawberry Water Improvement District ("District") and PWCo responds to the District's Response to Pine Water Company's Request for Stay docketed on June 4, 2009.

As the Commission is aware, the District signed an Order for immediate possession of PWCo and Strawberry Water Company ("SWCo"), which was entered by the Gila County Superior Court on May 5, 2009. That Order required the District to post a $3,200,000 bond and take possession of the water systems by May 22, 2009. Unfortunately, the District violated the Order for Immediate Possession by failing to post the bond and take possession of the water systems by May 22, 2009.

In turn, PWCo and SWCo filed a Motion for Sanctions with the Gila County Superior Court seeking sanctions against the District for its bad faith failure to comply

with the Order of Immediate Possession. The Motion for Sanctions is attached as exhibit A. That motion outlines PWCo's and SWCo's compliance with the Order of Immediate Possession and the District's violations of the Order. As stated in the motion, the District wasted the Superior Court's time and thousands of dollars of PWCo's and SWCo's attorneys' fees by seeking, negotiating and executing an Order for Immediate Possession and then failing to comply with its terms.

Incredibly, the District now seeks to waste the Commission's time and resources, as well as the resources and money of PWCo again, by opposing PWCo's request for stay in this docket. Apparently, the District wants the Commissioners, Commission Staff and PWCo to move forward with rate review proceedings for assets that the District intends to condemn in the pending Yavapai County Superior Court case.[1] The District's opposition to the stay is troubling because the District has stated its intent to proceed with the condemnation of PWCo and SWCo in Yavapai County Superior Court, which means that there is absolutely no reason to conduct rate review proceedings for PWCo.

Rather than acknowledge the obvious grounds for staying this docket, the District has opposed such stay and used its response as a means to throw mud at PWCo by claiming that PWCo "is clearly intending to be obstreperous and uncooperative and avoid providing information to PSWID." Unfortunately, that statement and the arguments contained in the District's Motion to Vacate Order for Immediate Possession simply aren't true. The simple truth is that the District failed to take possession of PWCo by May 22, 2009 because it never had financing available to take immediate possession. It's disingenuous for the District to claim in this docket that its violation of the Court's Order was caused by PWCo. That's not to mention that PWCo and SWCo fully complied with the express terms of the Order of Immediate Possession. *See* Motion for Sanctions at 5.

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[1] Pursuant to the Order of Immediate Possession, venue for the condemnation case was transferred to Yavapai County Superior Court.

Ultimately, for purposes of this docket, the Commission should learn from the District's violation of the Order for Immediate Possession and avoid expending unnecessary time and resources on rate review proceedings for assets that the District intends to condemn in the pending Yavapai County Superior Court case. Instead, the Commission should stay all outstanding compliance obligations indefinitely, including the rate review filing, pending final resolution of the condemnation proceedings.

DATED this 11 day of June, 2009.

FENNEMORE CRAIG, P.C.

By _____
Jay L. Shapiro
Todd C. Wiley
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Phoenix, Arizona 85012
Attorneys for Pine Water Company

ORIGINAL and 13 copies of the foregoing filed this 11th day of June, 2009 with:

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

COPY of the foregoing hand-delivered this 11th day of June, 2009 to:

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Phoenix, AZ 85007

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1200 W. Washington St.
Phoenix, AZ 85007

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Arizona Corporation Commission
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COPY of the foregoing mailed
this 11th day of June, 2009 to:

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By: Mary L Hauer
2205423/1/75206.006

EXHIBIT

A

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Attorneys for Defendants
Pine Water Co., Inc.; Strawberry Water Co., Inc.; Brooke Utilities, Inc.

SUPERIOR COURT OF ARIZONA

GILA COUNTY

PINE STRAWBERRY WATER IMPROVEMENT DISTRICT, a Tax Levying Public Improvement District, Plaintiff, v. PINE WATER CO., INC., an Arizona Corporation; STRAWBERRY WATER CO., INC., an Arizona Corporation; BROOKE UTILITIES, INC., an Arizona Corporation; COUNTY OF GILA, a political subdivision of the State of Arizona; JOHN DOES 1 through 10; and BLACK AND WHITE PARTNERSHIPS 1 through 10, Defendants.	No. CV2009-0785 **DEFENDANTS PINE WATER CO., INC.; STRAWBERRY WATER CO., INC.; AND BROOKE UTILITIES, INC. MOTION FOR SANCTIONS** (Oral Argument Requested)

Defendants Pine Water Co., Inc.; Strawberry Water Co., Inc.; and Brooke Utilities, Inc. (collectively "Defendants") hereby move for sanctions against Pine Strawberry Water Improvement District ("PSWID") for its bad faith and failure to comply with the Court's Order of Immediate Possession in this matter.

This is a condemnation case in which PSWID seeks to acquire two water systems owned by Defendants (one in Pine, Arizona and one in Strawberry, Arizona) that are

undisputedly worth millions of dollars. In its dealings with PSWID, Defendants have demanded for years that PSWID show it has the funding available to either purchase the systems or pay a judgment if it pursues condemnation. PSWID, however, has been unable to do so because it simply does not have the funding.

Nevertheless, PSWID recklessly charged forward with litigation to condemn the systems. Knowing that it did not have the financing or funds available to post a multi-million dollar bond to take immediate possession, PSWID recklessly and in bad faith filed an application for immediate possession, requested a hearing date, engaged in specific and detailed negotiations relating to possession, stipulated to possession, and had the Court enter an Order requiring PSWID to post a $3,200,000.00 bond and take possession by May 22, 2009. As the May 22, 2009 date approached, however, PSWID was finally forced to admit that it did not have, *and indeed never did have*, the financing or funds available to post the bond. PSWID orchestrated this entire fiasco knowing that it did not have the financing to perform at the time – misleading both the Court and Defendants into believing that it had financing in place.

PSWID's reckless actions have consequences. PSWID's lack of candor and misrepresentations to both the Court and Defendants have wasted hours of time, cost thousands of dollars in attorneys' fees and shown that PSWID is not financially sound enough to secure Defendants against any judgment or award of attorneys' fees if PSWID ultimately abandons this litigation. The Court should not tolerate such blatant bad faith and wasteful conduct. Pursuant to the Court's inherent powers, Defendants respectfully request that the Court sanction PSWID by: (1) awarding Defendants all attorneys' fees associated with PSWID's application for immediate possession and the negotiations, work and preparation caused by the application; (2) requiring PSWID to post a bond in the amount of Defendants' attorneys' fees and expert fees through trial for security in the event that PSWID abandons this action or cannot pay the ultimate judgment; and (3)

forcing PSWID to disclose to Defendants any and all information and documents they have regarding their purported financing for purchase or condemnation of the water systems.

I. Background

PSWID has sought to acquire the two water systems at issue for years. Unfortunately, however, PSWID has never had the financing in place to fund such an acquisition.

A. Defendants Demand Production of All Information Regarding PSWID's Proposed Financing For the Acquisition and PSWID Confirms It Does Not Have Financing or Funding Available.

After PSWID indicated that it intended to acquire the water systems through condemnation, on August 8, 2008, Defendants sent PSWID a request pursuant to Ariz. Rev. Stat. § 39-121.01(D), demanding any and all information relating to PSWID's financing and funding for the potential acquisition. In response, PSWID confirmed that it did not actually have financing in place – producing only a letter from an entity offering to try to help find financing for PSWID.

On September 25, 2008, Defendants again made a demand upon PSWID pursuant to Ariz. Rev. Stat. § 39-121.01(D) to produce any and all information relating to PSWID's financing and funding for the potential acquisition – including any and all information from the entity that was supposedly trying to help find financing. On October 9, 2008, PSWID again confirmed in response that it did not have financing in place and did not have any additional information on financing.

B. PSWID Files For Condemnation Despite Not Having Financing or Funding Available.

Despite not having financing in place, on November 12, 2008, PSWID filed this condemnation action to acquire the two water systems. PSWID did not seek to take immediate possession of the systems at that time.

In early February, the parties met to discuss a potential resolution of the case. As they have always done, Defendants demanded that PSWID show it actually had financing available to fund the condemnation. In response, PSWID showed Defendants a letter from Compass Bank that referenced a commitment letter dated February 5, 2009. *See* letter from Compass Bank (attached as Exhibit A). PSWID also showed Defendants a redacted form of a commitment letter, which included numerous terms and conditions for any potential financing. PSWID refused to let PSWID have a copy of the commitment letter or see an unredacted version. Based in part on PSWID's inability to show that it could fund a potential acquisition of the systems, settlement discussions were not successful.

C. PSWID Files An Application For Immediate Possession Despite Not Having Financing or Funding Available.

Despite not having financing or funding available, on March 25, 2009, PSWID inexplicably filed an Application for Immediate Possession and requested a hearing date on the application. The Court set the matter for a three-hour hearing for May 12, 2009. Defendants began preparing for the hearing spending significant resources associated with the same.

D. The Parties Spend Significant Time and Fees Negotiating a Stipulation to Immediate Possession.

Because PSWID would have to post a bond for several million dollars to take immediate possession, Defendants mistakenly believed that that PSWID was acting in good faith and would not waste the Court's and Defendants' time and resources by filing an application for immediate possession when it did not have financing available. Accordingly, Defendants offered to stipulate to immediate possession if the parties could agree on the amount of the bond and other conditions.

Beginning with Defendants' offer on March 27, 2009, the parties engaged in a lengthy series of negotiations on the terms for immediate possession. After significant effort, the parties were able to agree to the terms of possession and they filed a Stipulation to Order for Immediate Possession on April 24, 2009.

The terms of the stipulation were clear. Defendants would provide PSWID with:

> "(a) lists of their customers with names and addresses;
>
> (b) maps of the systems;
>
> (c) meter read dates and accounts receivable information; and
>
> (d) up to a total of 20 hours of time from [Defendants'] employees in the first two weeks after PSWID takes immediate possession (at a cost of $125 an hour to PSWID) to aid in transitioning the water systems at issue."

Order for Immediate Possession at ¶ 5. Defendants were not obligated to produce anything else. The stipulation and Order required PSWID to post a bond in the amount of $3,200,000.00 and take possession of the systems no later than May 22, 2009. *See* Order for Immediate Possession at ¶¶ 1-2.

The Court signed the Order for Immediate Possession on May 3, 2009, requiring PSWID to post the bond and take possession by May 22, 2009.

E. <u>Defendants Fully Comply With the Order for Immediate Possession and Prepare to Transfer Possession</u>.

Based on the parties' stipulation and the Court's Order, on May 7, 2009, Defendants provided everything required under the Order, including "lists of their customers with names and addresses, [] maps of the systems, [and] meter read dates and accounts receivable information" to PSWID. *See* Letter from Bart Wilhoit to John Gliege dated May 7, 2009 (attached as Exhibit B). Defendants also began preparing to transition the systems.

F. PSWID Confirms that It Will Violate the Order for Immediate Possession Because It Does Not Have Financing to Take Immediate Possession.

On May 13, 2009, PSWID sent a letter to Defendants complaining that in order to take immediate possession, it needed a host of other information that was not included in the stipulation and Order. *See* Letter from John Gliege to Bart Wilhoit dated May 13, 2009 (attached as Exhibit C). The letter indicated that, in violation of the Court's Order, PSWID would not take possession on May 22, 2009. *See id.*

Because Defendants had fully produced everything they were required to produce under the Order, Defendants grew concerned that the real reason PSWID was planning to violate the Court's Order was that PSWID did not have financing and, therefore, could not post the $3,200,000.00 bond on May 22, 2009. Accordingly, on May 13, 2009, undersigned counsel called PSWID's counsel and again demanded that PSWID prove that it had financing available to post the bond.

In response, PSWID confirmed that the real reason it could not take possession on May 22, 2009 as the Court Ordered was that it did not have financing to post the bond. PSWID's counsel wrote that PSWID did not have financing because "*in light of its concerns about the immediate possession concept [the bank] is not willing to fund immediate possession at this point in time.*" Email from John Gliege to Bart Wilhoit dated May 15, 2009 (attached as Exhibit D) (emphasis added). Counsel also attached a letter from the bank handling the purported financing in which the bank stated that it had never authorized any funding for immediate possession and would not do so:

> *Compass Bank is unwilling to amend its commitment to cover the Stipulation regarding immediate possession in view of a number of risks attendant to that process as well as other matters and developments relating to the District.*

Letter from Compass Bank to PSWID dated May 14, 2009 (attached as Exhibit E) (emphasis added). Clearly, PSWID had not secured anything other than the original

commitment from Compass Bank in February 2009 that was riddled with contingencies and never authorized funding for immediate possession. PSWID simply did not have financing for immediate possession.

G. PSWID Violates the Court's Order.

In response to PSWID's admission that it never had financing for immediate possession, Defendants warned PSWID that if it did not comply with the Court's Order, they would seek sanctions and damages associated with PSWID's actions. *See* Letter from Bart Wilhoit to John Gliege dated May 21, 2009 (attached as Exhibit F). Defendants also questioned why PSWID filed an application for immediate possession, requested a hearing date, engaged in specific and detailed negotiations relating to possession, stipulated to possession, and had the Court enter an order obligating PSWID to post a $3,200,000.00 bond and take possession by May 22, 2009 when it never had the financing to do so. *See id.*

PSWID never responded. Instead, on May 22, 2009, it simply failed to post the bond and take possession as ordered by the Court. Defendants retain possession of the systems and continue to operate them to serve the public.

II. Legal Analysis

The Court has inherent power to sanction bad faith and wasteful conduct in litigation. *See Precision Components, Inc. v. Harrison, Harper, Christian & Dichter, P.C.*, 179 Ariz. 552, 555, 880 P.2d, 1098, 1101(App. 1993) (citing *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43, 49, 111 S.Ct. 2123, 115 L.Ed.2d 27 (1991)). Similarly, the Court has power to punish contempt for a party's failure to comply with the Court's Order. *See Phoenix Newspapers, Inc. v. Superior Court In and For Maricopa County*, 101 Ariz. 257, 258, 418 P.2d 594, 595 (App. 1965); Ariz. Rev. Stat. § 12-864. In this case, PSWID has both acted in bad faith *and* intentionally violated the Court's Order. The Court should sanction PSWID by: (1) awarding Defendants all fees associated with PSWID's

application for immediate possession and the negotiations, work and preparation caused by the application; (2) requiring PSWID to post a bond in the amount of Defendants' attorneys' fees and expert fees through trial for security in the event that PSWID abandons this action or cannot pay the ultimate judgment; and (3) forcing PSWID to disclose to Defendants any and all information and documents they have regarding their purported financing for purchase or condemnation of the water systems.

A. The Court Should Award Defendants their Attorneys' Fees for All Work Associated with PSWID's Application for Immediate Possession, the Stipulation to Immediate Possession and Having to Bring this Matter Before the Court.

Not only does the Court have inherent authority to sanction PSWID by awarding Defendants attorneys' fees associated with PSWID's violation of the Court's Order as set forth above, but analogous common law and statutory authority provide support for such sanctions as well. A defendant in a condemnation action may recover fees and costs if the plaintiff did not act in good faith in "instituting" or "abandoning" condemnation proceedings. *State ex rel. Morrison v. Helm*, 86 Ariz. 275, 292, 345 P.2d 202, 206 (1959).[1] Courts require condemnors that act in bad faith to pay attorneys' fees because condemnation is a "heavy-handed power" that "impos[es] the expense of litigation on the defendant landowner." *Whitestone v. Town of South Tucson*, 2 Ariz.App. 494, 496, 410 P.2d 116, 118 (1966) (noting that a condemnor "should not proceed unless it has the set intention of paying the actual value of the property").

In this case, PSWID acted in bad faith in instituting proceedings to obtain immediate possession when it did not have funds or financing available to post the bond. It is axiomatic that PSWID could never take immediate possession of the systems at issue

[1] *See also* Ariz. Rev. Stat. § 12-1129(B)(2), stating that if a plaintiff "abandons" or dismisses a condemnation action, the defendant is entitled to an award of "costs, disbursements and expenses, including reasonable attorney, appraisal and engineering fees . . . ."

without posting a bond for Defendants' probable damages. *See* Ariz. Rev. Stat. § 12-1116(H). Although the parties have the opportunity to litigate what the amount of the bond should be for purposes of immediate possession, in this case, the parties compromised and stipulated that the amount of PSWID's bond would be $3,200,000.00. *See* Stipulation and Order for Immediate Possession.

PSWID knowingly and recklessly created this fiasco by charging ahead with immediate possession without having financing in place to see it through. PSWID's actions were in bad faith, deceptive to both Defendants and the Court and either grossly reckless or designed to manipulate the legal system. PSWID also violated the Court's Order.

Defendants spent significant time and effort in preparing for the immediate possession hearing, negotiating and finalizing a stipulation for immediate possession, preparing to transfer the systems at issue and bringing this matter to Court after PSWID violated the Court's Order. It is now clear that all of those efforts and attorneys' fees were wasted given that PSWID could never fund immediate possession. Because PSWID caused these actions by pursuing immediate possession when it knew it did not have financing to post the bond (and should have known it would never have financing to do so), the Court should sanction PSWID by awarding Defendants their attorneys' fees associated with PSWID's wasteful actions.

B. <u>The Court Should Require PSWID to Post a Bond in the Anticipated Amount of Defendants' Attorneys' Fees and Expert Fees Through Trial.</u>

Defendants are entitled to an award of attorneys' fees and expert fees if PSWID ultimately decides not to proceed with this action or if the Court determines that PSWID does not have the right to condemn the water systems. *See* Ariz. Rev. Stat. § 12-1129(B). As made clear by PSWID's recent admission of its inability to finance immediate possession, however, PSWID's ability to fund this litigation and pay Defendants' fees if

ordered to do so is extremely dubious. Compass Bank's unwillingness to finance immediate possession "in view of a number of risks attendant to that process" is almost certainly due to the fact that PSWID cannot guarantee Compass Bank what the price of the water systems will ultimately be – because that matter is left to the jury to decide. Indeed, Compass Bank's unwillingness to blindly finance PSWID's immediate possession is well founded given that millions of dollars are at issue and that in condemnation actions "[j]ury verdicts are notoriously known to vary considerably from conservative estimates . . . ." *Whitestone*, 2 Ariz.App. at 496, 410 P.2d at 118. If a jury ultimately awards an amount higher than what Compass Bank had anticipated, PSWID very likely will not have any financing to acquire the systems (or pay Defendants' attorneys' fees when they cannot proceed with the condemnation).

Given PSWID's illustrated blatant willingness to violate the Court's Orders, Defendants are left with *no* security in the event that PSWID decides not to proceed with acquiring the systems once a jury adjudicates their fair market value. As a sanction for creating that uncertainty by its recent misleading and bad faith conduct, the Court should require that PSWID post a bond from which Defendants can recover their attorneys' fees and expert fees in the event that, as it did in immediate possession, PSWID ultimately decides not to ultimately follow through with the condemnation. Defendants conservatively estimate attorneys' fees and costs through trial will be in excess of $300,000.00. Defendants request that the Court order a bond for that amount.

C. <u>The Court Should Require PSWID to Disclose all Documents and Information Associated with its Purported Financing</u>.

Finally, given PSWID's deceptive lack of candor with the Court and Defendants about its ability to finance the $3,200,000.00 bond for immediate possession, the Court should require PSWID to disclose all documents and information associated with its purported financing to Defendants (including, but not limited to, the amounts, terms and

conditions). Not only have Defendants been requesting that information for years, but it is also the subject of outstanding requests pursuant to Ariz. Rev. Stat. § 39-121.01(D) that Defendants submitted to PSWID before this litigation began. Based on the reckless, costly and misleading misadventure that PSWID put the Defendants and the Court through with immediate possession, both the Court and Defendants are entitled to know the exact terms and conditions of any purported financing so they can try to prevent PSWID from doing the same thing again.

III. Conclusion

Based on the foregoing, Defendants respectfully request that the Court sanction PSWID by: (1) awarding Defendants all fees associated with PSWID's application for immediate possession and the negotiations, work and preparation caused by the application; (2) requiring PSWID to post a bond in the amount of Defendants' attorneys' fees and expert fees through trial for security in the event that PSWID abandons this action or cannot pay the ultimate judgment; (3) forcing PSWID to disclose to Defendants any and all information and documents they have regarding their purported financing for purchase or condemnation of the water systems; and (4) awarding any other further sanctions as the Court deems appropriate.

DATED this 1st day of June, 2009.

FENNEMORE CRAIG, P.C.

By _____
Bart S. Wilhoit
Attorneys for Defendants
Pine Water Co., Inc.; Strawberry Water Co., Inc.; Brooke Utilities, Inc.

ORIGINAL of the foregoing filed this 1st day of June, 2009, with COPY mailed to:

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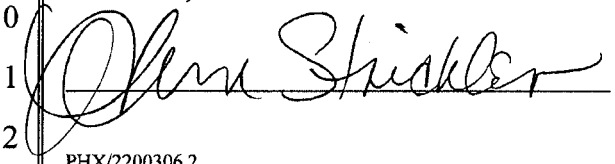

PHX/2200306.2

EXHIBIT A

Compass Bank

Payson/White Mountain Region
613 South Beeline Highway
Payson, Arizona 85541

Michael J. Whalen
City President
Private and Commercial Banking

February 5, 2009

Pine Strawberry Water Improvement District
Board of Directors
P.O. Box 134
Pine, Arizona 85544-0134

Re: Notice Commitment for Loan

Dear Board of Directors:

You have advised us that Pine Strawberry Water Improvement District (the "District") seeks financing (the "Loan") for the purchase and improvement of the used and useful assets of Pine Water Company, Strawberry Water Company, any assets of Brooke Utilities, or any third parties necessary for the operation of the domestic water systems within the areas presently served under the Certificates of Convenience and Necessity issued by the Arizona Corporation Commission to the Pine Water Company and the Strawberry Water Company and for other general corporate purposes (the "Project"). The amount of the Loan shall be within the amount set forth by the District and approved by Compass Bank for the acquisition and improvements to said system.

Based upon and subject to the terms and conditions set forth in that certain Commitment Letter (the "Commitment Letter") from Compass Bank ("Compass") to Borrower, Compass has issued the Commitment Letter dated February 5, 2009.

The terms and conditions of the Commitment Letter are confidential. Borrower may notify the proposed seller of the existence of the Commitment Letter. No third party shall be entitled to rely on the existence of the Commitment Letter or any of the terms and conditions set forth in the Commitment Letter.

Very truly yours,

COMPASS BANK, an Alabama banking corporation

By: Michael J. Whalen
Name: Michael J. Whalen
Title: City President

9449680.3

EXHIBIT B

FENNEMORE CRAIG, P.C.

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May 7, 2009

EM348484632US

Mr. John G. Gliege
Gliege Law Offices, PLLC
P.O. Box 1388
Flagstaff, AZ 86002

Re: *PSWID v. Pine Water Company, Inc. et al.*, Gila County Superior Court Case No. CV2008-375

Dear John:

As we discussed today, the Court signed the order for immediate possession. We received a copy yesterday. In case you haven't received a copy, I've enclosed a copy for you.

As we also discussed, attached are all of the documents we stipulated to produce in the order for immediate possession. PWC/00001-PWC/000091 are customer lists with names and addresses for the systems. PWC/00092- PWC/00093 are maps of the systems. PWC/00094-PWC/00184 are meter read dates and accounts receivable information. As we discussed, because PSWID plans on taking possession on May 22, 2009 pursuant to the order of immediate possession, we will do a final meter read for both systems on May 20 and May 21, 2009 (so that the parties will have an accurate depiction of the accounts receivable owed to Pine Water Co. and Strawberry Water Co. as of those dates and PSWID can start with a clean slate when it takes possession on May 22, 2009). We will provide you with an updated accounts receivable report after those final meter reads.

Additionally, as we discussed today, shortly before PSWID takes possession of the systems on May 22, 2009, Pine Water Co. and Strawberry Water Co. will remove the locks on all gates to well sites and well-houses because those locks are keyed the same as the rest of Brooke's other systems. PSWID can then use its own locks on all facilities.

Finally, please let me know whether PSWID wishes to condemn the water conversation stage signs we discussed for Pine Water Co. and Strawberry Water Co. There are six in Pine and five in Strawberry. If PSWID does not wish to condemn them, we will remove them after PSWID takes immediate possession on May 29, 2009. Thanks.

Sincerely,

FENNEMORE CRAIG, P.C.

Bart S. Wilhoit

PHX/2194542.1

EXHIBIT C

Gliege Law Offices, PLLC

John G. Gliege

May 13, 2009

Fennemore Craig, P.C.
Attn: Bart Wilhoit
3003 N. Central Ave, Ste 2600
Phoenix, AZ 85012-2913

Re: Pine Strawberry Water Improvement District Immediate Possession of PWC and SWC
Rule 408 Settlement Negotiations; this document is for settlement purposes only, fully subject to the terms and conditions of Rule 408, Arizona Rules of Evidence.

Dear Mr. Wilhoit:

The Board of Directors of the Pine Strawberry Water Improvement District (the "District") has been reviewing the progress being made regarding the District's immediate possession of the used and useful property of the Pine and Strawberry Water Companies. Since the time of the execution of the Stipulation regarding Immediate Possession there have been a number of materially significant issues which have arisen due to the actions or inactions of Pine Water Company, Strawberry Water Company or Brooke Utilities, which are jeopardizing the ability of my clients to fully perform their obligations as set forth in the Stipulation and which have the potential to jeopardize the public health, safety and welfare of the communities of Pine and Strawberry by creating water shortages over the forthcoming Memorial Day Weekend. If these issues are not resolved, or some other agreement not reached, the District will not be able to fully perform under the Stipulation. These include, but are not limited to:

1. In the process of moving out it appears that Pine and Strawberry Water Companies are leaving behind a number of ADEQ and ACC violations which the District will have to remedy at its cost. This is not acceptable. These include leaving in disrepair at least one major well, as well as some other problems with the water systems.

2. The minimal information which has been provided by Pine and Strawberry Water Companies thus far is insufficient to meet the stipulation requirements. Our initial review indicates that the information provided is woefully inadequate to provide for the operations of the water systems. For example, the data lists in some instances are at best randomly organized, or organized by first names of clientele. Further the lists do not address the location of the services nor do the maps provide a legend as to the meaning of the notations thereon. Furthermore some of the maps are not legible. No information was provided concerning meter sizes. There is no method to coordinate billing addresses with the service information and there do not appear to be service addresses or locations. Not all customers were reported on the lists. This incomplete information is an example of Pine

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E-mail: jgliege@earthlink.net

Water Company, Strawberry Water Company and Brooke Utilities' total disregard of the public health, safety and welfare of these communities.

3. The transition of the electrical power, water service, gas service, and telephone service as the same is involved in both the operations and in the telemetry for the operations of the District System from PWC and SWC to the District is not being concluded in an orderly manner The District understands that the Pine and Strawberry Water Companies have ordered the electric power turned off on the day of the District's immediate possession of the water systems, without providing the District any information as to how many meters are involved, their location and for what facilities such meters provide power. Further it is the District's understanding that the other utilities providing service to the water system will be terminated the same day leaving it impossible for the District to commence operations since no information has been provided concerning these utilities. Clearly this will impact the public health, safety and welfare of the communities.

4. The operation of the water systems and the telemetry equipment concerning the same is not being set up for a smooth transition. The District will have to be provided with the operations and maintenance manuals and the locations of the telemetry equipment for the operations of the water systems. It will also have to have the ability to convert this system to a District owned and operated system. Additionally the District needs the appropriate security information to ensure that all telemetry systems are safe from hackers or other mischief.

5. The District has been made aware of a dispute which one of the water companies is having with the owner of a particular well. The District has been made aware of the filing of a Motion to Intervene in the Condemnation proceedings by this individual. Since that dispute affects the used and useful property which is being taken by the District it is a significant matter. It is our understanding that that well in question provides more than ten percent of the water system supply. Therefore it is necessary for that issue to be resolved prior to the time the District takes immediate possession of the system.

6. There is also a concern about some aid in advance of construction agreements, which Pine/Strawberry Water Company may have entered into, collected money for, and not yet constructed the improvements. The District is taking the position that such agreements are not being transferred to the District; however the District is concerned about the impact of such agreements upon its constituency. The District understands that the handling of these matters would be up to the Pine/Strawberry Water Company to complete the work that they contracted to complete in a timely manner at the company's sole expense. Likewise if there are additional agreements to which PWC or SWC are a party concerning the construction of improvements, these too have to be fully resolved and the construction complete, or the money refunded to the payors or some other guarantee of the construction of the improvements provided.

7. Pine and Strawberry Water Companies have not responded to discovery requests in the condemnation matter which are due, and more responses are due next week.

Clearly the manner in which your clients, PWC and SWC are approaching this transition is not cooperative, but rather is an attempt to bring the operation of these systems to a standstill

during a busy holiday weekend, endangering the public health, safety and welfare. The District is extremely concerned about this and is commencing all necessary action to ensure that this does not occur.

In light of the foregoing, it is the intention of the District to immediately enlist the aid of the Arizona Department of Environmental Quality, the Arizona Corporation Commission, the Arizona Department of Water Resources, Gila County, the District's own powers to avert this public health issue as well as the Superior Court. It will file appropriate documentation with the other agencies described above immediately as well.

There appear to be a few alternative directions to go to rectify this situation. One is for the parties to fight out each and every one of these issues at considerable expense to the parties involved. A second is for the parties to stipulate to a final judgment of condemnation and final order of condemnation and provide for a smooth and orderly transition of the system to the District's ownership, operation or control. The amount of that stipulation to be the same as the amount set forth for the Immediate Possession of the systems. Without engaging in an appropriate cooperative effort to effectuate this transition the public health safety and welfare of the community is jeopardized and the District will not allow that to occur. This offer of complete settlement must be accepted within five days of the date of this letter. While it may take a few days past the May 22 date which was previously agreed upon for immediate possession to close this transaction, the orderly transition and the complete and final purchase of the systems will assure that the public health, safety and welfare of these communities are preserved.

If you have questions, then please contact this office.

Sincerely,
GLIEGE LAW OFFICES PLLC

/s/ John G. Gliege
John G. Gliege

EXHIBIT D

WILHOIT, BART

From: John Gliege [jgliege@earthlink.net]
Sent: Friday, May 15, 2009 12:45 PM
To: WILHOIT, BART
Subject: PSWID/PWC

Attachments: FAX of Bank letter 09 05 15.PDF

FAX of Bank letter 09 05 15.PD...

Bart, so far here is what I have been able to obtain from the Bank. Note, we have the money to close the whole transaction, but the bank, in light of what has occurred and in light of its concerns about the immediate possession concept is not willing to fund immediate possession at this point in time. I would suggest that we complete the transaction as a final condemantion and a full and complete purchase. If your client is willing to move forward on those terms, please advise.

John G. Gliege

EXHIBIT E

BBVA Compass

Private / Commercial Banking
613 S. Beeline Highway
Payson, AZ 85541
Phone 928-474-9679
Fax 928-474-4912

May 14, 2009

Mr. Harry Jones, Manager
Pine Strawberry Water Improvement District
P.O. Box 134
Pine, AZ 85544

Dear Mr. Jones:

This letter confirms that on April 28, 2009, William F. Haney, Board Chairman, executed a commitment letter with Compass Bank and presented a check payable to Compass Bank for the loan origination fee. Pursuant to its terms and conditions, the Compass Bank commitment provides for the timely acquisition of the Pine Water Company and the Strawberry Water Company from Brooke Utilities by the Pine Strawberry Water Improvement District.

Compass Bank is unwilling to amend its commitment to cover the Stipulation regarding immediate possession in view of a number of risks attendant to that process as well as other matters and developments relating to the District.

Very truly yours,

Michael J. Whalen
City President – Payson

EXHIBIT F

FENNEMORE CRAIG, P.C.

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Nogales (520) 281-3480
Las Vegas (702) 692-8000
Denver (303) 291-3200

May 21, 2009

VIA ELECTRONIC MAIL AND REGULAR MAIL

Mr. John G. Gliege
Gliege Law Offices, PLLC
P.O. Box 1388
Flagstaff, AZ 86002

Re: *PSWID v. Pine Water Company, Inc. et al.*, Gila County Superior Court Case No. CV2008-375

Dear John:

This letter responds to your correspondence dated May 13, 2009 regarding immediate possession and your subsequent correspondence regarding PSWID's discovery requests. It is apparent from that correspondence and our conversations that despite having filed an application for immediate possession, requesting a hearing date, engaging in specific and detailed negotiations relating to immediate possession, stipulating to immediate possession and having the Court enter an Order obligating PSWID to post a bond and take immediate possession by a specific date, PSWID does not have the financing, *and indeed never had the financing*, to take immediate possession of the systems. It is inexplicable that PSWID would engage in such conduct and breach of the Court's Order. At best, PSWID's actions associated with this condemnation are grossly reckless and uniformed. At worst, they are fraudulent and designed to disrupt service in the Pine and Strawberry service areas.

After we received your letter on May 13, 2009, I called your office to express our concern that PSWID was simply trying to back out of its obligation to take possession by May 22, 2009 because it did not have the money to post the bond for immediate possession. We demanded that PSWID prove it had the funds available to take possession and post the $3,200,000.00 bond as ordered by the Court.

In response, you confirmed that the real reason PSWID was unable to comply with the Court's order was that PSWID did not have financing. Indeed, you wrote that "in light of its

concerns about the immediate possession concept [the bank] is not willing to fund immediate possession at this point in time." May 15, 2009 Email from John Gliege to Bart Wilhoit. You also attached a letter from Compass Bank in which the bank itself confirmed that PSWID never had funding for immediate possession:

> Compass Bank is unwilling to amend its commitment to cover the Stipulation regarding immediate possession in view of a number of risks attendant to that process as well as other matters and developments relating to the District.

May 14, 2009 letter from Michael J. Whalen at Compass Bank to Harry Jones at PSWID. PSWID simply *never* had the funding available.

The Court entered the Order for Immediate Possession on May 3, 2009. Pursuant to the Order, PSWID is required to post a bond in the amount of $3,200,000.00 and enter into immediate possession "*on or before May 22, 2009*." The parties also specifically negotiated (and the Court ordered) *everything* that defendants were obligated to do to transfer possession. The Order states that defendants will provide: (1) lists of customer names and addresses; (2) maps of the systems; (3) meter read dates and accounts receivable information; and (4) up to 20 hours of defendants' time after immediate possession if requested by PSWID to aid in transition. Defendants have provided *everything* and remain willing to provide the transition time after PSWID takes possession. Unfortunately, PSWID has made it clear that it never had the financing available and that it intends to violate the Court's Order by not posting the bond or taking possession on May 22, 2009.

Given PSWID's lack of candor with defendants and the Court, PSWID's assertion that it cannot take possession due to defendants' actions is transparently self-serving and false. Defendants have complied with every single requirement set forth in the Order to date. Faced with the reality that it does not have financing and therefore cannot comply with the Court's Order, PSWID is trying to deflect its improper conduct by creating new obligations for defendants that exceed what is set forth the Court's Order. PSWID's actions show a lack of candor, an effort to manipulate the legal system, a lack of how the condemnation process works and a lack of understanding of the systems. The items listed in your May 13, 2009 letter are, frankly, either nonsensical or simply not required by the stipulation or Order.

Your statement that defendants' actions are "an attempt to bring the operation of these systems to a standstill during a busy holiday weekend, endangering the public health, safety and welfare" are reckless, entirely unsupported and libelous. It is even more incredible that you would make such inflammatory and untrue statements given your knowledge that PSWID was going to violate the Court's Order because PSWID never had financing for immediate possession. Defendants have fully complied with the Court's Order and expect PSWID to do the same. Rather than "endangering the public health," defendants have prepared to pick up the pieces of PSWID's inexcusable violation of the Court's Order. Defendants continue to operate

the Pine and Strawberry systems in the same manner they always have and will continue to serve the public if PSWID violates the Court's Order.

Given the lengths PSWID went to deceive defendants, the Court and the public in its failed experiment to take immediate possession, it is clear that PSWID is either extremely reckless or acting in bad faith. Under either scenario, its actions are not without consequence. While defendants will continue to serve the public if PSWID violates the Court's Order and fails to take possession, defendants will seek all remedies available to them for PSWID's actions – including seeking sanctions and damages, challenging PSWID's right to take the systems at issue and other available remedies.

Finally, we received your letter dated May 19, 2009 claiming that defendants' discovery responses to PSWID's interrogatories are overdue and that responses to PSWID's requests for production are due on May 24, 2009. You are incorrect on both accounts and your letter, purporting to be written pursuant to Rule 37, Ariz. R. Civ. P., is inappropriate.

PSWID served interrogatories on Pine Water Company and Strawberry Water Company by mail on April 2, 2009. In both sets of interrogatories, PSWID specifically states that responses are not due until "sixty (60) days from the date of service of this request." Sixty days from April 2, 2009 is June 1, 2009. Because the interrogatories were served by mail, an additional five days is added onto the response deadline pursuant to Rule 6(e), Ariz. R. Civ. P., extending the date until Saturday, June 6, 2009. Pursuant to Rule 6(a), Ariz. R. Civ. P., that date is extended until the first following business day. Accordingly, defendants' responses are not due until Monday, June 8, 2009 and defendants will respond accordingly.

With respect to the requests for production, your calculation of a due date of May 24, 2009 is also incorrect. The requests for production were served by mail on April 9, 2009 and requested responses within forty days. Forty days from April 9, 2009 is May 19, 2009. Because the requests were served by mail, an additional five days is added onto the response deadline pursuant to Rule 6(e), Ariz. R. Civ. P., extending the date until Sunday, May 24, 2009. Pursuant to Rule 6(a), Ariz. R. Civ. P., that date is extended until the first following business day. Taking into account the Memorial Day holiday, defendants' responses are not due until Tuesday, May 26, 2009 and defendants will respond accordingly.

Sincerely,

FENNEMORE CRAIG, P.C.

Bart S. Wilhoit