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1 BEFORE THE ARIZONA CORPORATION COMMISSION

2

3 IN THE MATTER OF THE APPLICATION OF)
 UTILITY SOURCE, L.L.C. FOR A) DOCKET NOS.
 4 CERTIFICATE OF CONVENIENCE AND) WS-04235A-04-0073
 NECESSITY TO PROVIDE WATER SERVICE) WS-04235A-04-0074
 5 IN COCONINO COUNTY, ARIZONA.)
)

6 IN THE MATTER OF THE APPLICATION OF)
 UTILITY SOURCE, L.L.C. FOR AUTHORITY)
 7 TO ISSUE PROMISSORY NOTE(S) AND)
 OTHER EVIDENCES OF INDEBTEDNESS)
 8 PAYABLE AT PERIODS OF MORE THAN)
 TWELVE MONTHS AFTER THE DATE OF)
 9 ISSUANCE.)
)

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11 At: Phoenix, Arizona

12 Date: October 12, 2004

13 Filed: **OCT 27 2004**

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REPORTER'S TRANSCRIPT OF PROCEEDINGS

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1 BE IT REMEMBERED that the above-entitled and
2 numbered matter came on regularly to be heard before the
3 Arizona Corporation Commission, in Hearing Room 1 of said
4 Commission, 1200 West Washington Street, Phoenix, Arizona,
5 commencing at 1:30 p.m. on the 12th of October, 2004.

6

7

BEFORE: Amanda Pope, Administrative Law Judge

8

9 APPEARANCES:

10

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CECELIA BROOKMAN, RPR
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1 ALJ POPE: We'll go on the record. Good
2 afternoon, welcome to the Arizona Corporation Commission.
3 This is the time and place set for the hearing in the
4 matter of the application of Utility Source, L.L.C., for a
5 certificate of convenience and necessity to provide water
6 and wastewater service in Coconino County, Arizona, as
7 well as the application of Utility Source, L.L.C. for
8 authority to issue promissory notes and other evidence of
9 indebtedness payable at periods of more than 12 months
10 after the date of issuance. The docket numbers are
11 WS-04235A-04-0073 and WS-04235A-04-0074.

12 My name is Amanda Pope and I'm the
13 administrative law judge assigned this matter. At this
14 time we'll take appearances of counsel, beginning with the
15 applicant.

16 MR. SALLQUIST: Thank you, Your Honor, let the
17 record show the appearance of Richard L. Sallquist on
18 behalf of the applicant Utility Source, L.L.C.

19 ALJ POPE: Thank you, Mr. Sallquist.
20 And for Staff.

21 MR. SABO: Tim Sabo, Your Honor, on behalf of
22 Staff.

23 ALJ POPE: Thank you, Mr. Sabo.

24 I will remind everybody again to ensure before
25 you're speaking that your green light is on on your

1 microphone so we can hear you.

2 Are there any procedural matters that we need
3 to discuss before we begin?

4 MR. SALLQUIST: I do not believe so, Your
5 Honor.

6 MR. SABO: That's my understanding as well.

7 ALJ POPE: Do you have an opening statement?

8 MR. SALLQUIST: The application before you
9 this afternoon is somewhat unique in certificate slash
10 financing applications. The company here started out as a
11 wholesale provider of water to a homeowners association
12 and a truck stop that are located in Bellemont, Arizona
13 and our prime witness, Mr. McCleve will lay the groundwork
14 as to how it was developed.

15 In the process of subdividing the property
16 that is being served, the developer obtained what's called
17 a letter of inadequacy from the Arizona Department of
18 Water Resources that basically indicates that given the
19 data that had been provided to them at that time, it could
20 not demonstrate a 100-year water supply for the
21 development as it was proposed.

22 In the process of -- and that letter of
23 inadequacy was then presented to the Arizona Department of
24 Real Estate, who then issued a property report indicating
25 that there was inadequate water supply. That's fine and

1 all in order with the Department of Real Estate
2 procedures.

3 In the process of developing the adjacent
4 land, the owners of the property learned that it was
5 necessary to file either an application for an
6 adjudication or a certificate of convenience and
7 necessity, and following meetings with the Commission
8 Staff, did in fact file the application that's before you
9 today.

10 Staff, in their review, determined that there
11 had in fact been issued a letter of inadequacy, which is
12 not the normal situation, in which this application
13 becomes somewhat unique. Normally those approvals from
14 ADWR are obtained at a later date. So the effect of the
15 letter of inadequacy basically put the certificate
16 application on hold.

17 After a series of meetings that the applicant
18 had with the DWR Staff, ADEQ, Arizona Department of
19 Environmental Quality staff, real estate staff, Commission
20 Staff, there were a number of meetings, and I think we
21 have now resolved how this matter can proceed, and
22 Mr. McCleve and I think Staff witnesses will speak to
23 that.

24 What we intend to present here today is a
25 letter from ADWR that basically indicates that the first

1 phase, if you will, of a little over half of the project
2 does in fact have adequate water. And we will also then
3 present the company's hydrologist who will testify that
4 his analysis, he believes there is water for the second
5 half, but we haven't proven it up with some of the finer
6 points at ADWR at this point.

7 So with meetings as recently as last week
8 among DWR staff, the Commission Staff and the company
9 representatives, it was agreed that we could proceed with
10 this if we had what is called the PAD, the physical
11 availability demonstration, from the Arizona Department of
12 Water Resources, which is the precursor, if you will, to
13 the letter of adequacy. There's just some financial
14 requirements and water quality things that need to be
15 provided subsequent to what we call the PAD, the physical
16 availability demonstration. Those need to be provided
17 before the physical and formal letter of adequacy is
18 completed.

19 So at our meeting last week, we were hopeful
20 that we would have all the information for the full blown
21 PAD. We have a letter that Mr. McCleve will testify to in
22 that regard. But based upon that status, we believe that
23 what the Commission Staff will recommend and what we are
24 now requesting is that the Commission issue either a
25 conditional certificate of convenience and necessity for

1 what we described as Phase I, or possibly an order
2 preliminary, depending on how Staff reads the letter that
3 we have from ADWR.

4 And then for the second phase of the project,
5 an order preliminary, Your Honor, that hasn't been used
6 recently by the Commission, but was used on a regular
7 basis in prior times. It's authorized under A.R.S.
8 40-284.D that contemplates the Commission basically saying
9 you've complied with these things, but you have to file a
10 number of additional things before we actually issue the
11 formal certificate, and the statute contemplates such
12 things as a franchise and other approvals with the
13 Commission has added on DWR approvals, ADEQ approvals and
14 those types of things.

15 But in any event, we're hopeful that we will
16 end up the day with a conditional certificate for Phase I,
17 an order preliminary for Phase II.

18 In addition to that, which I think is the
19 major issue in the matter before Your Honor today, the
20 company will present testimony in support for the hookup
21 fee, tariff that it supplied that Staff is not supporting
22 at this time.

23 Also, for the financing application that they
24 are recommending be denied, and also requesting that
25 instead of a rate application review filing for the test

1 year 2005, which is the first year of operation, that it
2 would be a more normal and we believe a more reasonable
3 approach to issue that five years, in the fifth year of
4 operation.

5 Your Honor, we will present two witnesses
6 today. Lonnie McCleve, M-c-C-l-e-v-e, who is the manager
7 of the applicant company, and also Gary Small, who is a
8 hydrologist with HydroSystems, Inc., and we will present
9 those two witnesses as well as the exhibits that we had
10 premarked, Your Honor.

11 ALJ POPE: Thank you very much. I want to ask
12 you really briefly, you had just said that with regard to
13 the pending rate case in the future, or the proposal of
14 the rate case, that you would propose it be based on the
15 fifth year of operation, and in your filing, which was
16 your response to Staff's, Staff report, you had also
17 mentioned the 2005 short form rate review. Are you
18 proposing that as well as an alternative?

19 MR. SALLQUIST: Yes, ma'am, and Mr. McCleve
20 will speak to that. I was trying to move along. Yes, we
21 think one or the other would be a reasonable approach in
22 lieu of the full application in year one.

23 ALJ POPE: Thank you.

24 Mr. Sabo, did you have an opening?

25 MR. SABO: Yes, Your Honor. And this is a

1 very unusual case, and in some ways a very troubling case,
2 but we are hopeful that we have reached an appropriate way
3 to resolve it and to move it forward.

4 What we have here is a company which
5 unfortunately commenced operations and was providing
6 service to customers without the certificate of
7 convenience and necessity that is required by law. And
8 obviously, that was a matter of great concern to the
9 Staff, and caused a number of problems throughout this
10 case.

11 And then the second problem was the fact that
12 they requested from DWR an expedited consideration of
13 their letter of adequacy, and that resulted in they got an
14 expedited determination, but the determination was that
15 there was insufficient water, which of course was somewhat
16 of a red flag for Staff, especially in this time of
17 drought that we are facing in this state.

18 So those are very difficult issues that the
19 Commission faces in this case. We believe that we do have
20 a way forward, based on numerous meetings that we've had
21 with the applicant as well as our fellow state agencies
22 over at the Department of Water Resources, Department of
23 Environmental Quality, and the Department of Real Estate.
24 We've been working together with those agencies, and of
25 course, we believe that government agencies should try and

1 work together to benefit the public good, and we think we
2 have an appropriate solution here today. And as you are
3 probably aware, in our Staff report we did recommend
4 denial of the CC&N. We will be revising that
5 recommendation based on these further developments and
6 further meetings.

7 What we will be recommending is that there's
8 an area which Mr. Sallquist has called Phase I. It's an
9 area described in greater detail in the letter from DWR
10 that is marked as Exhibit A-10. That area, if they can
11 obtain a PAD or physical availability determination from
12 Arizona Department of Water Resources, that area described
13 in the DWR letter, we will recommend that a regular
14 conditional CC&N be granted for that area.

15 If they are unable to obtain a PAD for that
16 area, then we will recommend that an order preliminary be
17 issued for that area conditioned upon obtaining the PAD.

18 And then for the remaining area of the
19 application beyond what is described in the DWR letter, we
20 would recommend simply an order preliminary that would
21 require them to come back with a PAD as well as all the
22 other usual conditions being satisfied, such as franchises
23 and so forth.

24 And I would note the order preliminary, as
25 Mr. Sallquist has said, is something that we have not done

1 in quite a long time. It is expressly contemplated in the
2 statute. And actually, the correct citation for that is
3 40-282.D, so Mr. Sallquist was off by two as sometimes --

4 MR. SALLQUIST: Thank you, I was close.

5 MR. SABO: -- sometimes happens to all of us.

6 And that particular statute does explicitly
7 contemplate the Commission issuing these types of order
8 preliminary orders.

9 So that's what we will recommend in this case,
10 that a CC&N be granted if they can get a PAD for this area
11 described in the DWR letter. And we would -- we will
12 consent to their submitting that PAD as a late-filed
13 exhibit. And then for the remaining area, an order
14 preliminary conditioned on a PAD franchise and the other
15 normal conditions.

16 How the order preliminary works is that it
17 lists certain things that you have to do, and then when
18 the applicant comes back and submits those things, it
19 actually has to go back before the Commission, and the
20 Commission has to enter a formal order finding that they
21 have satisfied those conditions. So you don't have,
22 currently with a conditional certificate, there's that
23 null and void language that just kind of automatically
24 pops out of existence. Instead of having it automatically
25 happen, the Commission actually has to physically enter an

1 order, so it's a little more cleaner and clearer on the
2 record whether there is a CC&N or not.

3 So those are the areas where we think we have
4 reached an agreement with the company. There are a few
5 other areas where there are still disagreements with
6 regard to the rates. Unfortunately, we are forced to
7 recommend a somewhat substantial increase in the rates.
8 Part of the problem is that the company's current rates
9 are not set to cover the type of costs that the company is
10 going to be incurring, and so it's not unusual that a
11 developer starts out with kind of lowball rates to
12 encourage people to come in and then they have to be
13 raised later. We don't want to run into that situation or
14 at least endorse that situation. We think appropriate
15 rates need to be set from the onset here at the
16 Commission.

17 With regard to the recommendation for the rate
18 case, Staff normally recommends that they come back with
19 five years of operations. As I mentioned, unfortunately,
20 this company has already been operating without a CC&N, so
21 our recommendation, under our recommendation for a 2005
22 test year, that will provide five years of operations
23 because of their prior operations before they had the
24 CC&N.

25 With regard to the financing, quite simply,

1 they don't have enough money to pay, to cover the debt
2 that they're proposing to incur. And then secondly, it's
3 somewhat troubling because they're proposing to get this
4 money as a loan from the developer. That's an affiliated
5 transaction, obviously, and it would be more appropriate,
6 instead of the developer getting guaranteed repayment as
7 debt as the investor in this project, for that money to be
8 treated as capital, and as investment in the company.

9 And the same issue also arises with a hookup
10 fee, that it's appropriate for the owner, for the person
11 controlling the company, to make a real substantial
12 investment in the company and for that reason, we're not
13 recommending a hookup fee. Likewise, for a number of
14 policy reasons, we simply do not recommend hookup fees for
15 initial CC&Ns, and that's not the case here.

16 So those would be Staff's recommendations.
17 Staff will present them through testimony of Mr. Jim
18 Fisher. And that concludes my opening statement.

19 Thank you.

20 ALJ POPE: I'm sorry to ask you a question,
21 but I just want to clarify.

22 MR. SABO: Sure.

23 ALJ POPE: The first recommendation that you
24 stated with regard to the company being able to obtain the
25 PAD for Phase I, and you said that you would consent to

1 them filing that as a late-filed exhibit. Does Staff have
2 a time frame in which they would like to see that done?

3 MR. SABO: Your Honor, based on our
4 conversations with DWR, we believe that the issuance of
5 that PAD is relatively imminent in the next week or two.
6 The letter that's marked A-10 is kind of a preliminary
7 step towards a PAD. We do believe that it will be
8 forthcoming fairly shortly.

9 We had thought about putting a time frame in
10 there. However, due to our desire to work cooperatively
11 with other state agencies, we did not want to put a hard
12 and fast deadline in there. Instead, if at anytime the
13 company is able to come forward with a PAD, we would
14 recommend that the CC&N go ahead, be granted for that area
15 described in the DWR letter.

16 ALJ POPE: Thank you.

17 I apologize for not asking earlier whether
18 there was any public comment before we proceeded with
19 opening statements. I don't see any, so we'll go ahead
20 and have you call your first witness.

21 MR. SALLQUIST: Thank you, Your Honor. I
22 would like to call Lonnie McCleve and ask that he be
23 sworn.

24 (Lonnie McCleve was duly sworn.)

25 MR. SALLQUIST: Your Honor, as I indicated, we

1 Q. And again, for the record, would you please
2 explain generally where the subject property is located.

3 A. Flagstaff Meadows is located in Bellemont,
4 Arizona, which is approximately eight miles west of
5 Flagstaff off I-40, Exhibit 185.

6 Q. It's right adjacent to the freeway there?

7 A. It is.

8 Q. Mr. McCleve, I show you what has been marked
9 as Exhibit A-1 and ask if that is in fact the certificate
10 of convenience and necessity application filed by the
11 company on January 30th, on your behalf.

12 A. It is.

13 Q. And referring to what has been marked as
14 Exhibit A-2, is that in fact the companion financing
15 application filed that same day?

16 A. Yes.

17 Q. And during the Staff's discovery in their
18 analysis of those applications, did they ask for certain
19 additional information, including your updated and revised
20 capital costs associated with the utility plant?

21 A. They did. And we provided them some
22 additional information that showed an updated, what our
23 updated costs have been for our infrastructure for the
24 water and sewer treatment system.

25 Q. Referring to what has been marked as Exhibit

1 A-3, is that in fact the Staff's first data requests and
2 your response thereto, including that updated information?

3 A. Yes, it is.

4 Q. Referring to Exhibit A-4, is that the
5 affidavit of the notice that was required by the
6 procedural orders in this matter?

7 A. Yes.

8 Q. And those have been duly filed with the
9 Commission docket and control?

10 A. They have.

11 Q. The capital costs that you have included in
12 Exhibit A-3, those updated capital costs, are those the
13 current capital costs that the Commission Staff utilized
14 in their Staff report?

15 A. Yes, I believe it is.

16 Q. Will you briefly summarize the elements of
17 both the certificate application and the financing
18 application.

19 A. Well, I believe the certificate application
20 is, I'm not an expert in there, but basically our
21 application is to get a certificate of convenience and
22 necessity to provide water to individuals as a franchised
23 water company.

24 Q. And it included an application for certain
25 rate levels and certain hookup fees associated with

1 providing that service?

2 A. It did.

3 Q. And then what was the substance of the
4 financing application?

5 A. The financing application was basically, if I
6 recall, a \$525,000 request that we anticipated would be
7 used as a line of credit for the utility, they would meet
8 shortfall requirements, and we saw that it would be
9 something that would be paid back and forth on a somewhat
10 regular basis.

11 Q. We'll speak to that in a little more detail
12 later.

13 Again, kind of setting the stage here, I'd
14 like to refer to what has been marked as Exhibit A-5 and
15 ask if that is a map of the area that you are requesting
16 to be served.

17 A. It is, yes.

18 Q. And referring to Exhibit A-6, is that a
19 three-page legal description of that same property?

20 A. Yes. And it describes it in a couple of
21 different ways, based on some previous discussions that we
22 had.

23 Q. Mr. McCleve, you have a demonstrative exhibit
24 of A-5 here, do you not?

25 A. Yes.

1 Q. The eight and a half by eleven copies have
2 been circulated to the parties.

3 Referring to Exhibit A-6, three pages, the
4 first page is entitled legal description, Utility Source,
5 truck stop, motel and undeveloped?

6 A. Right.

7 Q. Would you please indicate on the demonstrative
8 exhibit where those parcels that are on Page 1 are
9 located. Please try and verbalize it, because the court
10 reporter is trying to take this down, and stand so the
11 parties can see what you're pointing to.

12 A. This area that is marked in green is the area
13 that is described under the first legal description
14 Utility Source, truck stop, motel and undeveloped.
15 Utility Source is where the basic water system is, and
16 that's where the well fields are, where all of the wells
17 are located.

18 Q. That area is included in what we are asking,
19 and will later describe as Phase I, the first 325 units
20 that we're going to get the PAD for?

21 A. It is.

22 Q. So that's Page 1 of Exhibit 6?

23 A. That's correct.

24 Q. Now, if you turn to Page 2 of Exhibit 6, it's
25 titled legal description, Flagstaff Meadows I and II,

1 Townhomes I, sewer treatment plant and fire station.

2 Again, pointing to the demonstrative exhibit
3 in Exhibit A-5, will you please describe where that is
4 located.

5 A. The second page includes all of the existing
6 platted areas which would be Flagstaff Meadows I and II,
7 Flagstaff Meadows Townhomes, and the sewer treatment plant
8 and a fire station site, which is up in this corner right
9 here.

10 Q. Is it safe or fair to say that that includes
11 the lots that are platted in the blue and in the purple
12 and in the green?

13 A. Yes, and including the Bellemont fire station,
14 which is outlined with a kind of a beige color.

15 Q. Then if you would show the judge where the
16 treatment plant is located.

17 A. The treatment plant is right down here.

18 Q. And that will serve the entire area?

19 A. That's correct.

20 Q. Likewise, the area you describe from Page 1 in
21 the upper left-hand corner of Exhibit A-5, the wells and
22 all are located in that general area?

23 A. Yes. The wells are located where it says,
24 it's marked by Utility Source.

25 Q. Now, the areas that you've just described are

1 the areas that you will later testify you have the PAD
2 for, and are what we've been referring to as the 325
3 Phase I lots; is that correct?

4 A. Yes.

5 Q. Now, referring to Page 3 of Exhibit A-6,
6 titled Flagstaff Meadows I, II, and III, Townhomes I and
7 II, sewer treatment plant, Bellemont commercial and the
8 fire station, would you please describe what that
9 represents on the demonstrative exhibit.

10 A. That legal description includes everything
11 except the green area.

12 Q. Everything that was described, except what was
13 described on Page 1?

14 A. That's correct. It would include what was on
15 Unit II, plus what we're calling our second phase, the
16 unplatted areas.

17 Q. So the entire area that you're requesting is
18 encompassed on Page 1 and Page 3 --

19 A. That's correct.

20 Q. -- of Exhibit A-6?

21 A. That's correct.

22 Q. Mr. McCleve, let me back up a little bit and
23 get some of the history of the company here. Would you
24 please explain to the judge how you first became involved
25 in the Bellemont area.

1 A. I purchased the truck stop that is located
2 there. I purchased it approximately in 1995, operated it
3 for a number of years. I kind of saw what the market was
4 like, and as a matter of fact, we had a number of
5 employees that were working there, and there was a great
6 need for quality, affordable housing, and we started to
7 deal with that issue. We saw some property that was
8 available to the east of the truck stop that we had
9 located, and purchased some additional property.

10 Q. And the truck stop had both a water supply and
11 some wastewater capacities needed for the truck stop?

12 A. It did.

13 Q. And were the capacities of those systems able
14 to serve any area beyond or larger than the truck stop?

15 A. From a water point of view, we were able to
16 supply more than what we had right there at that point.
17 The sewer treatment plant, in order to serve it with
18 sewage capability, we had to do a number of things. We
19 had to go to ADEQ and apply for a NPDES permit so that we
20 could have a discharge for effluent. We also had to get
21 an APP permit from ADEQ and all of their other permits.

22 Q. When you noticed this adjacent land that was
23 available, you purchased it and proposed to put some
24 residential development on it?

25 A. I did.

1 Q. And how were you proposing that they would
2 obtain utility services?

3 A. They were obtaining utility service by buying
4 wholesale water from the truck stop well system. And the
5 truck stop was actually selling to the homeowners
6 association, and the homeowners association was providing
7 water to the individual customers.

8 Q. This was a relatively small development at
9 that time?

10 A. Correct.

11 Q. And you are now providing wholesale to that
12 homeowners association; is that correct?

13 A. We are.

14 Q. Approximately how many customers are you
15 serving at this time?

16 A. There's approximately 200 right now.

17 Q. And would you please explain why and how those
18 customers received utility service prior to Utility Source
19 receiving a CC&N.

20 A. Well, as I was saying, we provided wholesale
21 water to the homeowners association, the homeowners
22 association turned around and billed them individually,
23 and that's the way we received it.

24 Q. Was it your understanding that wastewater
25 service could be provided without any regulation through a

1 nonprofit entity?

2 A. Yes.

3 Q. And that the water service for that small
4 property was in a sense incidental to the provision of the
5 other homeowner services?

6 A. It would be, yes.

7 Q. Was it ever your intent to avoid the
8 jurisdiction of this Commission or any other agency in
9 providing that service?

10 A. No, no.

11 Q. So you have worked extensively with other
12 agencies to try and obtain all the appropriate approvals?

13 A. Yes. I worked with ADEQ, ADWR, Department of
14 Real Estate, and all of the things that they require in
15 order to get public for it.

16 Q. In hindsight, Mr. McCleve, do you believe it
17 probably would have been more appropriate to seek a
18 certificate of convenience and necessity from this
19 Commission?

20 A. Yes.

21 Q. Again, you just were not aware of the
22 requirements until you started expanding the area?

23 A. It actually came up in Phase II, is when the
24 issue came up.

25 Q. So explain for the judge how you became aware

1 of the fact that you needed to obtain either an
2 adjudication or a certificate of convenience and
3 necessity.

4 A. When we recorded -- when we were going for
5 approval for Unit II -- and Unit II would be the
6 single-family homes and the townhomes here -- and as we
7 were getting approval from ADEQ, we got our approval, but
8 it was told to us that we needed to get Arizona
9 Corporation Commission approval at that point. And we
10 heard, ADEQ I think contacted the Corporation Commission,
11 they in turn contacted us, and we had a meeting with them
12 where we discussed what our options were, and there were
13 options of going for adjudication or a franchise CC&N.
14 And it was obvious the way that it needed to be done is to
15 get the CC&N.

16 Q. Now, did you contact any other utility
17 providers in the area to see if an existing company was
18 available to provide those services?

19 A. There's only one other utility in the area,
20 and that's the Bellemont Water Company. They have very
21 limited water capabilities, but -- and they have no sewer
22 capabilities, so that really wasn't an option.

23 Q. And you have provided in this application a
24 letter from Bellemont Water Company that says they're not
25 able to provide either of those services; is that correct?

1 A. I have, yes.

2 Q. So in the development process, you formed a
3 homeowners association and set forth in the covenants,
4 conditions, and restrictions the terms and conditions of
5 providing the water and wastewater services; is that
6 right?

7 A. Yes.

8 Q. And then you were -- you had subdivided that
9 first phase, have you not?

10 A. Yes.

11 Q. What approvals had you obtained -- had you
12 obtained Real Estate Department approval for this
13 subdivision?

14 A. Yes. We obtained all the approvals. The
15 jurisdiction is Coconino County, we got their approval, we
16 got ADEQ approval, you know, all of the various agencies
17 within the county.

18 Q. What representations did you make to the
19 Arizona Department of Real Estate regarding the water
20 supply in the Phase I?

21 A. They saw the CC&Rs, so they knew exactly what
22 we were doing, that we were getting wholesale water from
23 the homeowners association.

24 Q. They were aware of the HOA as the provider?

25 A. Yes.

1 Q. What about the adequacy, DWR approvals for the
2 subdivision?

3 A. It's interesting, because it seems like the
4 other agencies look at the water adequacy or inadequacy
5 very differently than the way that the Corporation
6 Commission looks at it.

7 The only thing -- what they require is that we
8 get a determination from ADWR. And in order to get that
9 determination from DWR, you have to get a physical
10 availability study, which we didn't do at that point. So
11 if you don't do that physical availability study, then you
12 automatically get an insufficiency letter. If you get the
13 insufficiency letter, then what they require is that you
14 disclose it on your public report to any individual that's
15 purchasing water.

16 Q. So there's no prohibition against selling
17 those lots, it's merely the disclosure that there's
18 inadequate supply?

19 A. Yes.

20 Q. Did ADEQ look at the adequacy of the water?

21 A. Yes.

22 Q. What was their conclusion?

23 A. Their conclusion was the water was there.

24 Q. So then after you did the Phase I with the
25 letter of inadequacy, I assume that that subdivision was

1 successful?

2 A. It was.

3 Q. You decided you wanted to expand the
4 subdivision into a little larger area?

5 A. Yes.

6 Q. Did you make application to the then
7 appropriate agencies for that extended subdivision?

8 A. We did. We went through the same process we
9 had gone through on Phase I.

10 Q. What response did you get when you made the
11 representation regarding water supply and the like on that
12 second phase?

13 A. Are you talking about from DWR?

14 Q. Yes, sir, or from Real Estate, either one.

15 A. Again, we had not done the necessary study in
16 order to prove water supplies, so because you don't prove
17 it, then they deem it inadequate.

18 Q. Then who was it that first advised you, of
19 those agencies, that you would need to have a public
20 service corporation as a provider?

21 A. ADEQ. At our approval, at ADEQ's approval is
22 where we were notified of that.

23 Q. And then about that same point in time did you
24 receive a formal notification from the Commission Staff
25 that you needed to make either an application for

1 adjudication or CC&N?

2 A. I did.

3 Q. And how did the company respond to that?

4 A. We almost immediately, after we had that
5 conversation with them, we prepared and submitted the
6 application that I think is your A-1.

7 Q. Prior to submitting that, though, you did have
8 a meeting with the Commission Staff --

9 A. We did.

10 Q. -- to discuss the alternatives of adjudication
11 and a certificate?

12 A. We did.

13 Q. And you concluded the certificate was the way
14 to go?

15 A. Yes.

16 Q. And then as you indicated, as a result,
17 Exhibit A-1 was filed?

18 A. That's correct.

19 Q. Did you continue serving the existing
20 customers in that phase at the time you submitted the
21 application?

22 A. We did.

23 Q. And then you continued to serve the second
24 subdivision that was again incorporated into the
25 homeowners association and the controlling CC&Rs?

1 A. Yes.

2 Q. And subsequent to that were you contacted by
3 the Commission Staff regarding that additional service?

4 A. We were.

5 Q. And what was the result of that contact?

6 A. Basically, what they said is that what they
7 wanted us to do is not provide service to any additional
8 customers that weren't already hooked up. We were told
9 any existing customers, we were to continue supplying
10 them, but to not hook up any additional customers.

11 Q. The company was formally notified of that
12 continued existing service, and ceased future service, in
13 a letter from Mr. Sabo on March 22nd of 2004; is that
14 correct?

15 A. That's correct.

16 Q. And again, to clarify that, did you have
17 additional meetings with the Commission Staff about what
18 were, in fact, quote, existing customers as of March 22nd?

19 A. We did. And we had a clarification of that.
20 They were kind enough to work with us, and provide us with
21 letters basically showing the actual lot notes for
22 existing customers.

23 Q. So you had provided lot numbers and plat maps
24 as to who you actually served as of that date?

25 A. That's correct.

1 Q. And they confirmed that back to you saying
2 that these, I believe it was 201 lots are your, quote,
3 existing customers that you can continue to serve?

4 A. I'm not sure of the number, but yes, yes, I
5 did.

6 Q. Was it your impression that during a normal
7 ramp up, if you will, from an unregulated HOA to a
8 regulated company, that that would be a permissible
9 practice that you serve those customers?

10 A. The existing customers?

11 Q. Yes.

12 A. My understanding is that from the letters that
13 we had received from them that we were required to serve
14 the customers.

15 Q. Mr. McCleve, who owns the underlying land
16 that's demonstrated there on Exhibit A-5?

17 A. Entities that I'm associated with.

18 Q. So it is controlled by virtually you or other
19 entities that control that property?

20 A. Yes, it is.

21 Q. And is it basically fully developed at this
22 point?

23 A. No. You're talking about the whole map?

24 Q. Yes.

25 A. No. There's several areas that are not --

1 well, even in the platted areas, there's a number of lots
2 that are not built on, until this CC&N issue is resolved,
3 and there's areas that are not even platted yet.

4 Q. The Staff report, I believe, stated that it
5 thought there was going to be a golf course or some large
6 turf customer. Is it your intent to have a golf course in
7 this area?

8 A. No.

9 Q. Has your hydrologist assumed that there would
10 not be a golf course in his analysis?

11 A. Yes.

12 Q. And do you anticipate any commercial customers
13 beyond the existing truck stop and hotel?

14 A. We would anticipate that when the subdivision
15 is close to being built out, that there would be a demand
16 and a need for commercial development in the area, and
17 there's a piece that is set aside for that purpose.

18 Q. Is it a significant area? Do you believe that
19 will have a significant water demand?

20 A. We would see that as being a small water
21 demand based upon commercial uses rather than residential
22 uses.

23 Q. Mr. McCleve, I'd like to have you find Exhibit
24 A-3, if you would, which is the Commission Staff's data
25 request and our response. I believe it's the cover,

1 there's a letter from my office dated August 10th.

2 A. I've got it.

3 Q. If you will turn about seven or eight pages
4 from the back of that exhibit, there are a couple
5 schedules, one called Schedule 8 and one called
6 Schedule 9. They're on a landscape format. Have you
7 found those?

8 A. Yes.

9 Q. The first one, Schedule 8, is estimated water
10 costs. Is that in fact your best estimate of what the
11 backbone facilities for water are going to be for this
12 developed area?

13 A. Yeah, I believe that's what we've spent to
14 date.

15 Q. So this plant is in the ground, this, I
16 believe in the right-hand column, about two-thirds of the
17 way down, shows like \$2.4 million?

18 A. Yes.

19 Q. And that includes the shallow wells and the
20 deep wells and the pumps and tanks and all that's
21 necessary for the service to this area?

22 A. It does.

23 Q. Then if you'd flip to the next page,
24 Schedule 9, there again, that's for the wastewater, and in
25 a similar location it shows \$1.4 million?

1 A. Yes.

2 Q. 1.39?

3 A. Yes.

4 Q. That is the plant. Again, that plant is in
5 place at this date?

6 A. It is.

7 Q. And the on-site facilities listed below that
8 are the subdivision costs that are not what you call
9 backbone; correct?

10 A. That's correct.

11 Q. Who owns the assets that presently provide
12 water to this area?

13 A. They're actually held by a couple of different
14 partnerships that are in there. What our intent is,
15 assuming that we get a successful CC&N, we would agree to
16 deed all of these to the Utility Source, L.L.C. upon the
17 receipt of the CC&N.

18 Q. So it will be investor investment or
19 membership interests in the L.L.C.; is that correct?

20 A. That's correct.

21 Q. And then how will the future capital
22 requirements be funded?

23 A. We would -- what we had intended is that it
24 would be a combination of loans from Greenfield Land
25 Development, from the developer of the area, and the sewer

1 and water hookup fees is what we had proposed.

2 Q. So the on-site facilities, not loan but line
3 extension agreements, will be fundable agreements, in
4 utility parlance, the on-site subdivision pipes will be
5 paid for by the developer?

6 A. That's correct.

7 Q. And then the hookup fee that you're proposing
8 would in effect fund the future expansion for the
9 additional wells, treatment plant modules, and such?

10 A. Right. Which is the normal way that I'm used
11 to dealing with municipalities, that that's the way they
12 pay for the infrastructure, so that individuals that are
13 building homes, that they're paying for the actual costs
14 of the water and sewer capacity.

15 Q. Subject to check, would you agree that the
16 application contemplates approximately \$1.3 million in
17 additional capital investments?

18 A. Yes.

19 Q. And based upon the hookup fees that you
20 proposed, for the 625 or 75 lots will it generate
21 approximately the number of dollars that are needed to
22 support that?

23 A. It would.

24 Q. And do you recall for the judge what the level
25 of hookup fee is that you're proposing for water and

1 wastewater?

2 A. We had mirrored what was existing as our
3 closest neighbor, which is Flagstaff. It's an \$1800 sewer
4 fee and \$1,000 water fee for a total of \$2800.

5 Q. That is, as you indicated, the fees that the
6 City of Flagstaff is charging for their new hookups?

7 A. That's correct.

8 Q. What is the basis for your belief that that is
9 an appropriate level of hookup fee for this company?

10 A. Well, as you look at the numbers, and we have
11 done that, and the costs of putting those prime
12 improvements in, that isn't anywhere close to covering the
13 cost of it, but it's a benefit towards it.

14 Basically we looked at other municipalities
15 and what their rates are. And many of them down in the
16 valley, in this area, are much higher than that, but it
17 seemed like a reasonable beginning for them.

18 Q. Now, the Staff is normally concerned about
19 start-up companies having hookup fees, because as you may
20 be aware, hookup fees end up reducing the rate base of the
21 company. Staff's concern, I believe, is that if you have
22 too many hookup fees, you will reduce the investors'
23 equity in the company to the point that it has virtually
24 no rate base so it has nothing to earn return, so it gets
25 cash starved. Will that be the case in this company?

1 A. In this case, we've already invested, if you
2 add these up, we've got over, close to \$4 million invested
3 already, so basically, the hookup fees would act as a
4 catalyst for helping us to expand.

5 Q. And they will not, if you took the entire,
6 call it a million and a half dollars in hookup fees, and
7 reduce the rate base by that amount, it would not leave
8 you without a rate base, would it?

9 A. Oh, no.

10 Q. Again, the hookup fees anticipated to be
11 generated at your level will raise approximately the
12 revenues, I'm sorry, the capital requirements for this
13 future growth that you're expecting?

14 A. Yes.

15 Q. I'd like to refer back to the financing
16 application, Exhibit A-2, for just a moment.

17 Staff points out that you haven't sought any
18 equity approvals for the approximately \$4 million that you
19 say you invested in the company. Why have you not sought
20 approval of the equity portion of the company?

21 Let me lead you a little bit. Does it have to
22 do --

23 A. I think you need to --

24 Q. This is a limited liability company as opposed
25 to a corporation?

1 MR. SABO: Objection. A, leading; and B, it
2 sounds like he's going to offer some type of legal
3 analysis of the requirements of the Commission which I'm
4 not aware of whether that has been established that he's
5 competent to testify on that area.

6 MR. SALLQUIST: That's fair, Your Honor, I'll
7 rephrase it.

8 ALJ POPE: Thank you.

9 Q. BY MR. SALLQUIST: Mr. McCleve, was it your
10 opinion that it was not necessary to obtain Commission
11 approvals of limited liability company interests in the
12 traditional financing applications before the Commission?

13 A. Yes.

14 MR. SABO: Same objection as to what he's
15 aware of, or -- there's been no foundation as to whether
16 he would be aware of something, or if he was aware of it,
17 what the basis of his understanding would be.

18 MR. SALLQUIST: I'm merely asking his opinion,
19 Your Honor.

20 ALJ POPE: I think you answered yes. I'll
21 allow that.

22 Q. BY MR. SALLQUIST: Regarding the short-term
23 line of credit that you're asking, the \$525,000, how do
24 you envision the company drawing on and repaying that line
25 of credit, and why is it necessary, in your opinion, to

1 have that?

2 A. We feel that that would act as a shortfall for
3 us in between collecting hookup fees, that sort of thing,
4 and it would be a means of us lending money to the utility
5 so that the financing is in place to meet any shortfall
6 needs. We didn't anticipate that it would be, that it
7 would encumber any of the assets. It would be more like a
8 line of credit, is what we had envisioned.

9 Q. And the \$525,000 also built into the exhibits,
10 including the cash flows that are set forth in the
11 application, was based upon the assumption that the
12 Commission would grant rates substantially in the form of
13 what you requested; is that correct?

14 A. Yes.

15 Q. And Mr. Sabo had alluded to it. The
16 Commission Staff is in fact recommending rates
17 substantially higher than what you had asked for; is that
18 correct?

19 A. Yes. And if in fact that is what transpires,
20 we would anticipate that we would be using a lot less,
21 obviously, of that note or that line of credit, whatever
22 you want to call it. We would be using a lot less of it.

23 Q. Have you made any computation as to what that
24 would be?

25 A. No. I haven't looked at their rates and put

1 it into our need as well.

2 Q. The need for the funds may be similar, but
3 with the higher rates is it conceivable that those funds
4 would be paid sooner than you contemplated?

5 A. Yes, we would anticipate they would,
6 obviously.

7 Q. In the event you don't have a short-term line
8 of credit and you need to make these additions that you've
9 contemplated in your application, how would the company
10 fund those plant additions?

11 A. I guess you would do it as equity.

12 Q. And if there were hookup fees in place, there
13 wouldn't be the ability to use those to repay the loan; is
14 that correct?

15 A. I believe so, yes.

16 Q. Again, in the application you provided your
17 best estimate of what the property expenses of the water
18 and wastewater division would be; is that correct?

19 A. Yes.

20 Q. To the best of your knowledge, has Staff taken
21 exception to any of those estimates?

22 A. Not to my knowledge.

23 Q. And based upon those, you designed a rate that
24 you propose in the application?

25 A. Yes.

1 Q. And I think you may have alluded to this, at
2 least when you were talking about the hookup fees. Are
3 the rates that you're proposing similar to the rates that
4 are utilized by the City of Flagstaff?

5 A. They mirror them.

6 Q. And again, can you share with the judge
7 approximately what you believe to be the water division's
8 operating expenses in year one?

9 A. The shortfall or the --

10 Q. No, just the total operating expenses.

11 A. Total expenses. I believe they're about
12 \$100,000.

13 Q. And is it safe to say that the wastewater
14 expenses are slightly more than that on an annual basis?

15 A. I believe so, yes.

16 Q. And those were your estimates of those
17 expenses at the time you filed the application in January
18 of '04?

19 A. Yes.

20 Q. And you still believe them to be fairly
21 accurate?

22 A. I do.

23 Q. If you have Exhibit A-1, Mr. McCleve, the
24 application. I think most of you have copies that are
25 tabbed, and I'd refer to what is tabbed No. 5 and ask you

1 if that is the tariff the company is proposing.

2 A. It is.

3 Q. Again, that would set forth the rates that you
4 had proposed, not the Staff's rates; is that correct?

5 A. That's correct.

6 Q. And it incorporates the terms and conditions
7 of your hookup fee?

8 A. Yes.

9 Q. And does it contain a form of cross connection
10 or backflow control tariff?

11 A. I believe so, yes.

12 Q. And how about a curtailment plan type tariff?

13 A. I believe there is in there.

14 Q. Those may need some refinement, the backflow
15 and the curtailment may need some refinement based upon
16 Staff's revisions to those form of tariff; is that
17 correct?

18 A. That's correct.

19 Q. But you believe Tab 5 to Exhibit A-1 is an
20 appropriate form of tariff for this company?

21 A. I do, yes.

22 Q. We talked about it a little bit in the opening
23 and the judge asked about it a little bit. The Staff is
24 recommending the company file a full rate application
25 based upon the test year 2005. We had filed exceptions

1 and commented on what we believed the appropriateness of
2 that. Would you please comment on whether or not you
3 believe a full-blown rate application is appropriate in
4 your first year of operation.

5 A. Well, it feels like there would be some
6 extraordinary expenses that might occur in the first
7 start-up year. There could be some things we're not even
8 aware of, accounting expenses. I know there's a number of
9 things that are going to change, so it would probably be
10 beneficial if we could do that a little further down the
11 road.

12 Q. Would you have any objection to filing what
13 the Commission Staff calls a short-form application,
14 basically as a several page summary of the financial
15 information that they could determine whether or not at
16 that point a full application would need to be filed?

17 MR. SABO: Your Honor, I'm going to object to
18 this line of questioning on the grounds that it has not
19 been established that Mr. McCleve has any expertise in the
20 area of ratemaking, and therefore he's not qualified to
21 testify as to ratemaking matters.

22 MR. SALLQUIST: Your Honor, I'm not asking
23 Mr. McCleve the specifics of ratemaking. I think he does
24 understand and we'll ask him about the accounting
25 requirements that are imposed on a company with a

1 certificate.

2 But I think he's certainly qualified as an
3 ongoing businessman to know that the costs associated with
4 a rate case would certainly be more than a rate review, as
5 the Commission Staff defines it. I'm not asking the
6 particulars of rate applications, Your Honor.

7 ALJ POPE: To the extent that you're
8 testifying to the company's willingness to file
9 alternatives in a future rate application case before the
10 Commission, I'll allow that, but let's not go beyond that.

11 MR. SALLQUIST: I think I'm there, Your Honor.
12 Thank you.

13 Q. BY MR. SALLQUIST: Mr. McCleve, again, the
14 Staff is suggesting that the company would file all the
15 approvals to construct from the Arizona Department of
16 Environmental Quality. Are you familiar with that
17 requirement?

18 A. I am.

19 Q. Again referring to Exhibit A-1, the
20 application, Tab No. 7, does that in fact represent the
21 approvals to construct and approvals of construction that
22 you had received as of the time of the filing of the
23 application?

24 A. They do.

25 Q. And have you subsequently received any

1 additional approvals of construction?

2 A. We have.

3 Q. Referring to what has been marked as Exhibit
4 A-7, are those in fact two additional AOCs?

5 A. I don't have that in front of me.

6 MR. SALLQUIST: May I approach the witness,
7 Your Honor.

8 ALJ POPE: Sure.

9 Q. BY MR. SALLQUIST: What is represented by
10 Exhibit A-7?

11 A. Those are -- they're certificate approvals of
12 sanitary facilities for Flagstaff Meadows Unit II and
13 Flagstaff Meadows Townhomes.

14 Q. Now, will that constitute all of the approvals
15 that you will need to obtain from ADEQ for the facilities
16 that you're building in this requested area?

17 A. That covers all of the platted areas, yes.

18 Q. So what you're saying is that the Unit III and
19 the Phase II townhouses that have not yet been platted,
20 you do not have those approvals?

21 A. No, I do not.

22 Q. Again, there's been a little discussion this
23 afternoon about the Arizona Department of Water Resources
24 approvals. I would like to refer you to what has been
25 marked as Exhibit A-8, which is my transmittal letter to

1. Mr. Olea, a binder. Would you please explain what Exhibit
2 A-8 represents?

3 A. What I have is not the entire binder, but I
4 have the --

5 Q. I'm sorry, I may have mismarked them.

6 Your Honor, did I mark a two-page color sheet
7 as Exhibit A-8?

8 ALJ POPE: I have A-8 as the binder, and I
9 have A-9 as the spreadsheet you're referring to.

10 MR. SALLQUIST: I think that's correct.

11 Q. BY MR. SALLQUIST: Mr. McCleve, that's A-9.
12 A-8 is this binder. Referring to that, would you please
13 explain to the judge what that is and how you got to the
14 point you were needing such a binder?

15 A. At ADWR's request, and in order to prove
16 adequate water for the subdivisions that we're proposing
17 and building, it's a requirement to prove the water. PAD
18 stands for physical availability determination. And we
19 hired HydroSystems, Gary Small and Sheila Ehlers with
20 HydroSystems to put that together, to basically determine
21 whether the physical availability of water was there or
22 not for a 100-year period of time.

23 Q. And that analyzes the demand that the proposed
24 development will need in the way of water and the supply
25 of available water; is that correct?

1 A. It does.

2 Q. Is that report -- and Mr. Small will testify
3 to it momentarily, but does that report demonstrate the
4 adequacy for the water in the area?

5 A. We believe it does, yes.

6 Q. Referring to what has been marked as Exhibit
7 A-9, is that some supplemental information regarding this
8 analysis that HydroSystems has filed?

9 A. It is.

10 Q. Again, Mr. Small will speak to that?

11 A. Yes.

12 Q. Exhibit A-10 is a letter addressed to you from
13 Doug Dunham. Would you please explain a little bit of
14 background on that, and what that letter represents and
15 how it was obtained?

16 A. Basically, as we had been working with the
17 Department of Water Resources, they have verbally
18 indicated to us that they believe that there is a physical
19 availability of water there, at least to the point of
20 109.46 acre feet, which is the amount that is required for
21 what I would call all of the platted areas and the
22 existing facilities and the platted areas in this
23 certificated area.

24 In their process of doing that, there is -- we
25 have found that it is something of a lengthy process to

1 obtain that. They have, at our request, given us a status
2 of where they are as far as issuing a physical
3 availability determination, and this letter is that status
4 letter. Basically, the way I interpret it, it's saying
5 that it's imminent that they're going to issue it, and
6 they're just telling us it's down the road.

7 Q. But this is not the physical availability
8 determination?

9 A. It is not.

10 Q. And do you have any sense of the timing of
11 when the actual physical availability determination will
12 be made?

13 A. I spoke with Mr. Dunham this morning and he
14 indicated that within a week he would have it. Hopefully
15 sooner, but within a week is what he had told me.

16 Q. You could and will file that exhibit, if Your
17 Honor permits, as a late-filed exhibit in this proceeding?

18 A. I will.

19 Q. And with that physical availability, what
20 areas on Exhibit A-5, the entire certificated area, what
21 area will have a physical availability determination?

22 A. Shall I point to the map?

23 ALJ POPE: Please.

24 THE WITNESS: It would be this area that's
25 marked in green, and then it would be everything that is

1 platted, which would be this area here. Basically, it's
2 everything on the map, with the exception of the area in
3 brown and the Bellemont commercial. So that is not
4 included.

5 Q. BY MR. SALLQUIST: The area you're excepting
6 is what we're also referring to as the Townhomes Phase II,
7 and the Unit III; is that correct?

8 A. That's correct.

9 Q. And approximately how many platted units are
10 in that, quote, Phase II?

11 A. Approximately 350.

12 Q. And in the Phase I, then, there are a total of
13 how many?

14 A. Total, there's 325.

15 Q. And you understand Staff's recommendation that
16 in the event you can provide that letter of physical
17 availability from the ADWR, that they would be supportive
18 of the Commission issuing what's known as a conditional
19 certificate of convenience for that area?

20 A. That is my understanding.

21 Q. Now, what more would you need to do to get the
22 PAD for what we're calling Phase II?

23 A. We would enlist HydroSystems' assistance in
24 further proving our water capability.

25 Q. Mr. Small will expand on that requirement of

1 that?

2 A. He would. There's a number of ways of doing
3 it but we have a plan in place as to how we want to
4 approach that, and we think it's cheaper.

5 Q. And what is your understanding of what it is
6 that Staff is recommending that the Commission do with a
7 certificate for that, what we're calling Phase II at this
8 point?

9 A. My understanding is that it would be a, I'm
10 forgetting the words, preliminary -- order preliminary
11 that would basically enable us, once we prove physical
12 availability of water, that we would be able to be granted
13 the CC&N for that area also. But until that, that it
14 would be basically in limbo, is what I'm understanding,
15 until that occurs.

16 Q. But you would not have to file a new
17 certificate extension application. Once you met the
18 requirements of the order prelim, the Commission would
19 reconsider that, Staff would make its recommendation, and
20 then the Commission would initial an additional order?

21 A. That's correct.

22 Q. Do you have any sense of the timing -- maybe
23 Mr. Small is a better witness for this -- as to the timing
24 of when you might be able to get the PAD for Phase II?

25 A. It depends somewhat on how we approach it.

1 One of the things that we're in the process of doing is
2 doing some surveying for another potential well, and if
3 the surveying comes out the way that we hope it might, it
4 could be very quickly. It depends on how we approach it.
5 We've talked about the recharge permit, and it sort of
6 depends on how that occurs. We would think three months
7 to a year.

8 Q. Three months to a year?

9 A. Yes.

10 Q. Moving to some of the nitty-gritty here, who
11 is going to provide the day-to-day management and
12 operation in the company?

13 A. We have an individual employee who is there
14 on-site and he will continue to be there. But in addition
15 to that, we have a certified operator that will continue
16 to be there.

17 Q. Is the certified operator an employee or is it
18 a contracted?

19 A. Contracted.

20 Q. Will there be a local office there?

21 A. Yes.

22 Q. Are you aware of the unique accounting
23 requirements for utility companies as well as the
24 requirements imposed by the Commission rules and
25 regulations and tariffs on a utility company?

1 A. We are learning that. We know that there are
2 some requirements.

3 Q. And you're familiar with the various reporting
4 requirements the utility has, both to the Commission and
5 ADEQ and DWR and other regulatory agencies?

6 A. We are, yes.

7 Q. And will you represent to this Commission that
8 you will comply with those requirements?

9 A. I will.

10 Q. I think you obviously had a chance to look at
11 the Staff report?

12 A. Yes.

13 Q. And what is your conclusion regarding the
14 Staff report?

15 A. Well, they're changing part of it because
16 they're talking about issuing an order preliminary, I
17 guess, for the CC&N. We obviously think that we should
18 have a CC&N issued. To me, it makes sense to have a sewer
19 and water tap hookup fees. That let's the developer slash
20 customer pay for some of the direct expense of expansion,
21 which seems a fair way to deal with rates, and which would
22 tend to lower the costs of the utilities to the existing
23 customers, so I think that makes sense.

24 To me it makes sense that we would have a loan
25 in place where we could draw on it, and pay it back on an

1 as-needed basis, to fund the shortfall of the company. So
2 I mean basically, those are my comments about the Staff
3 report.

4 Q. With those couple three exceptions, you
5 basically agree with the Staff report?

6 A. Yes.

7 Q. Were Exhibits A-1 through A-10 basically
8 prepared at your direction?

9 A. Yes.

10 Q. And in your opinion, is there a public need
11 and necessity for granting a certificate of convenience
12 and necessity to utility service to provide water and
13 wastewater service in this area at this time?

14 A. Yes.

15 Q. In your opinion, is Utility Source a fit and
16 proper entity to hold a certificate of convenience and
17 necessity?

18 A. Yes, it is.

19 Q. Will the proceeds of the financing be used for
20 lawful purposes that are within the powers of the company?

21 A. Yes.

22 MR. SABO: Objection as to lawful, as it calls
23 for a legal conclusion.

24 MR. SALLQUIST: Your Honor, there is -- that
25 is correct. The statutes do designate and specify certain

1 conclusions that the Commission order in a financing
2 application would reach. I believe Mr. McCleve can
3 express his opinion as to whether or not what he's
4 proposing is lawful. Ultimately, the determination is
5 made by the Commission, but I think he can express his
6 opinion as to whether or not it's lawful.

7 MR. SABO: I would say that the witness is not
8 qualified to offer a legal opinion. Insofar as I'm aware,
9 he's not an attorney licensed in this state or any other
10 state. And in any event, if he was an attorney, I don't
11 believe that legal opinions are the proper subject of
12 expert testimony, but rather would be for a legal argument
13 by counsel.

14 MR. SALLQUIST: That's fine, Your Honor. I'll
15 withdraw the question.

16 ALJ POPE: Okay.

17 Q. BY MR. SALLQUIST: Is the financing compatible
18 with the public interest, with sound financial practice
19 with the proper performance of a service by a public
20 service corporation?

21 A. I believe so.

22 Q. Will the financing impair the company's
23 ability to perform its public service obligations?

24 A. No.

25 Q. Are the proceeds of the financing to be

1 reasonably chargeable to operating expenses or to income?

2 A. No.

3 Q. If they were to be, would it be for the
4 purposes that you stated, for the temporary funding of
5 those operations?

6 A. Yes, it would be a shortfall.

7 Q. What is the timing for the need of the
8 Commission to act on your proposed project here?

9 A. It would be nice if it was very soon.

10 Q. Is the proposal that Mr. Sabo and I have
11 discussed in our opening statements regarding the issuing
12 of the conditional certificate for the Phase I and the
13 order preliminary for Phase II an acceptable process and
14 procedure for you, the investors and property owners up
15 there?

16 A. It is.

17 MR. SALLQUIST: Your Honor, I'd like to offer
18 Exhibit A-1 through A-10 into evidence at this time.

19 ALJ POPE: Did you have any objections?

20 MR. SABO: Yes, Your Honor, I think I do. It
21 may be helpful to go through them one by one since some of
22 them I not, and some I do have an objection to.

23 ALJ POPE: Okay.

24 MR. SABO: With regard to A-1, no objection.

25 With regard to A-2, also no objection. No objection to

1 A-3. No objection to A-4, the affidavit of publication.

2 With regard to A-5, the map, and A-6, the
3 legal description, I guess we would object as to proper
4 foundation. But I think that can be cleared up if
5 Mr. Sallquist asks if those items accurately reflect the
6 area up there. So hopefully that one can be cleared up
7 pretty simply.

8 A-7, Your Honor, I don't believe the witness
9 has mentioned A-7, so at this point I'm not sure what
10 basis there would be.

11 MR. SALLQUIST: Those are the approvals of
12 construction. I think he did testify to them.

13 MR. SABO: Okay, no objection to that one.

14 With regard to A-8, the application, and A-9,
15 the spreadsheet or chart, those both appear to go to the
16 matter of water supply, which I do not believe that the
17 witness is qualified. And I understand that they intend
18 on presenting a hydrologist, so I think it would be more
19 appropriate if they were admitted under the hydrologist.

20 MR. SALLQUIST: I concur with that, Your
21 Honor.

22 ALJ POPE: Okay.

23 MR. SABO: With regard to A-10, the DWR
24 letter, no objection.

25 ALJ POPE: Did you want to direct your

1 questions, Mr. Sallquist, to your client with regard to
2 A-5 and 6?

3 MR. SALLQUIST: If I might.

4 Q. BY MR. SALLQUIST: Mr. McCleve, referring to
5 Exhibit A-5, which is the plat map of the area, and
6 Exhibit A-6, the legal description for the areas, do those
7 accurately reflect the area that you are requesting to be
8 or proposing to be included in the certificate?

9 A. They do.

10 Q. And the various phasings that are set forth in
11 Exhibit A-6?

12 A. They do.

13 MR. SALLQUIST: Does that work Mr. Sabo?

14 MR. SABO: Fine with me. No objection to A-5
15 and A-6.

16 ALJ POPE: Okay. So A-1 through A-7 are
17 admitted and A-10 is admitted as well.

18 MR. SALLQUIST: Thank you, Your Honor.
19 Mr. McCleve is available for cross-examination.

20 ALJ POPE: Okay.

21 Mr. Sabo, did you have any questions?

22 MR. SABO: I do, Your Honor. I was wondering
23 if this would be a convenient time for a short break.

24 ALJ POPE: We'll take a 10-minute recess.

25 (A recess ensued.)

1 ALJ POPE: We're back on the record.

2 Mr. Sabo, you were going to give us some
3 cross-examination.

4 MR. SABO: Yes, Your Honor, thank you.

5

6

CROSS-EXAMINATION

7 BY MR. SABO:

8 Q. Good afternoon, Mr. McCleve.

9 A. How are you doing?

10 Q. All right. Yourself?

11 A. We're doing well.

12 Q. Okay. Hopefully I won't change that too much.

13 Sir, do you have any prior experience running
14 a water company?

15 A. No, I do not.

16 Q. You're not familiar, then, with the technical
17 requirements that relate to running a water company?

18 A. When I say no, I do not, that's really not
19 exactly correct. I've operated the water system for the
20 truck stop that has been in place since '95. I've done
21 all of the reporting that is required under ADEQ
22 requirements to deal with that, and I've been familiar
23 with the expenses and the ongoing operation of that water
24 and the sewer treatment plant that was there.

25 Q. Is that truck stop a residential public water

1 system?

2 A. It is not.

3 Q. So you have no experience running a
4 residential public water system?

5 A. No, I do not.

6 Q. Let's talk about the assets in question for a
7 minute. You mentioned the current investment in those
8 assets is around \$4 million; is that correct?

9 A. Somewhere in that area, yes.

10 Q. And you mentioned that the assets were owned
11 by a variety of affiliated entities that you're related
12 to; is that correct?

13 A. Yes, it is.

14 Q. Could you nail that down a little bit for us,
15 who owns what?

16 A. Part of it is owned by a L.L.C. called Fuelco
17 Travel Center. The rest of it is owned by Greenfield Land
18 Development, L.L.C.

19 Q. And which of those entities owns which assets?

20 A. Fuelco Travel Center owns the area marked
21 under Utility Source on the map. Greenfield Land
22 Development owns where the sewer treatment plant is
23 located.

24 Q. Are you talking about land, or assets like
25 mains and so forth?

1 A. The land and assets would be the same, same
2 ownership.

3 Q. And who owns the distribution mains?

4 A. Greenfield Land Development.

5 Q. Okay. And is Greenfield Land Development,
6 what is that, a corporation, an L.L.C.?

7 A. It's an L.L.C.

8 Q. Likewise with Fuelco Travel Center?

9 A. That is an L.L.C. also.

10 Q. And these two L.L.C.s, who owns the equity or
11 controlling interests in those L.L.C.s?

12 A. I do.

13 Q. Is that 100 percent ownership, sir?

14 A. 80 percent in the -- on behalf of Greenfield
15 Land Development, and with regard to Fuelco, it's 97
16 percent.

17 Q. Likewise, the land that underlies all this
18 area, who owns that land?

19 A. Well, the lots that have been sold are
20 individuals that own homes, so we wouldn't own any of
21 that. The lots that are not built on in Flagstaff, what I
22 would describe the lots that are not built on in Flagstaff
23 Meadows Unit II, Greenfield Land Development would own
24 those. The lots that are not built on in the townhomes at
25 Flagstaff Meadows, those are owned by Empire Development.

1 Flagstaff Meadows Unit III is owned by an
2 L.L.C. called Flagstaff Meadows, L.L.C., and then this
3 approximately 30 acres on this section towards the west
4 end of Flagstaff Meadows Unit III is owned by Greenfield
5 Land Development pension plan.

6 Q. So the, you mentioned Greenfield Land
7 Development, L.L.C., that's the same L.L.C. that you own
8 80 percent of; is that correct?

9 A. That's correct.

10 Q. And again, exactly which lots do they own or
11 which area do they own? Excluding, of course, the ones
12 that have already been sold.

13 A. Greenfield Land Development, L.L.C. would own
14 in what we would call as Flagstaff Meadows Unit II, the
15 undeveloped lots in there; Greenfield would own those.
16 And then Greenfield would own the sewer treatment plant,
17 and I guess that's it.

18 Q. Okay, and then you mentioned for the
19 townhomes, that it was owned by some entity called Empire
20 something?

21 A. Empire Development, I believe is.

22 Q. Is that also an L.L.C.?

23 A. I'm not sure. I think it is.

24 Q. And this Empire Development, who owns the
25 equity in that?

1 A. It's a California corporation. The principal
2 of it is a gentleman named Jim Prevaty.

3 Q. Do you have some relationship with this Empire
4 Development?

5 A. We do.

6 Q. And what would that relationship be?

7 A. We had developed lots and sold developed lots
8 to them in Flagstaff Meadows Unit I and in Flagstaff
9 Meadows Unit II. In regard to Flagstaff Meadows
10 Townhomes, we actually sold them the raw land, and they
11 put the roads and infrastructure in, so they developed the
12 raw lots themselves.

13 Q. By "we," you're talking about Greenfield Land
14 Development, L.L.C.?

15 A. Yes, I'm sorry.

16 Q. And so therefore, the townhomes development
17 that is owned by Empire Development, that's being
18 developed in conjunction with Greenfield Land Development,
19 L.L.C.?

20 A. It is.

21 Q. And Greenfield Land Development, L.L.C. kind
22 of set that project up?

23 A. Yes. We did the basic planning for it and we
24 did some of the zoning for it, and then they took it from
25 there.

1 Q. And then you mentioned Flagstaff Meadows,
2 L.L.C. Remind us again what area they own.

3 A. It is this area, which would be the western --
4 it would be the easternmost area of what we're calling our
5 third phase of Flagstaff Meadows III, and it's a
6 combination of the single-family, which is Flagstaff
7 Meadows III, and Flagstaff Meadows Townhomes. I know this
8 is confusing, I apologize, but it would be the easternmost
9 part of that.

10 Q. In this Flagstaff Meadows, L.L.C., who owns
11 the equity interest in that?

12 A. I do.

13 Q. Is that 100 percent?

14 A. 80 percent.

15 Q. Who owns the other 20 percent?

16 A. Gary Bulechek.

17 Q. Likewise, who owns the other 20 percent of
18 Greenfield Land Development, L.L.C.?

19 A. Gary Bulechek.

20 Q. Who is this Mr. Bulechek?

21 A. He's here in the audience.

22 MR. SABO: Hello, sir.

23 MR. BULECHEK: Hello.

24 Q. BY MR. SABO: He's a business associate of
25 yours, I take it?

1 A. He is.

2 Q. And then lastly, you mentioned additional area
3 that was owned by you called Greenfield Land Development
4 pension something?

5 A. It's owned by the -- by our pension plan,
6 which is the Greenfield Land Development pension plan.

7 Q. And that pension plan is the pension plan for
8 the Greenfield Land Development, L.L.C.; is that correct?

9 A. That's correct.

10 Q. It is then controlled by yourself as well as
11 Mr. Bulechek?

12 A. It's the same ownership, yes.

13 Q. Remind us again what area the pension plan
14 owns?

15 A. It would be the westernmost 31 acres of -- it
16 would include the Bellemont commercial, and approximately
17 21 acres of Flagstaff Meadows III and Flagstaff Meadows
18 Townhomes II.

19 Q. Why was this placed in the ownership of the
20 pension plan as opposed to the Greenfield Land
21 Development, L.L.C.?

22 A. Because we had purchased it at a different
23 time. It was fractured ownership prior to us putting
24 those together. Basically, what we've done is put those
25 several pieces of property together. There were several

1 different owners involved.

2 Q. Now, you mentioned there's a homeowners
3 association up there; is that correct?

4 A. There is.

5 Q. Tell me a little bit about how the homeowners
6 association runs. In particular, in my experience, tell
7 me if this is the case here, but in my experience, it's
8 often the case the developer sets it up so that until a
9 large majority of lots are sold, effective control of the
10 homeowners association remains with the developer.

11 A. That is correct.

12 Q. So that's the case here?

13 A. Yes.

14 Q. So at this point in time, the homeowners
15 association is under your effective control; is that
16 correct?

17 A. It is.

18 Q. And let's turn then to the Utility Source,
19 L.L.C. Who owns the equity interest in that?

20 A. It is the same ownership, 80 percent,
21 20 percent.

22 Q. So you own 80 percent, and the other
23 individual, Mr. Bulechek owns 20 percent?

24 A. That's correct.

25 Q. Is it fair, then, to say that the homeowners

1 association, Utility Source, Greenfield Land Development,
2 Greenfield Land Development pension plan, and Flagstaff
3 Meadows, L.L.C. are all affiliated entities that are under
4 common control?

5 A. Yes.

6 Q. Thank you.

7 Let's talk a little bit about the ADEQ. Let
8 me see if I understand your testimony. Basically, my
9 understanding is that you testified that basically, you've
10 got all these approvals from ADEQ; is that correct.

11 A. Yes.

12 Q. And I handed out some exhibits up there that
13 should have been marked S-3 and S-2. Do you see those?

14 A. I do.

15 Q. And do those appear to be documents with the
16 Arizona Department of Environmental Quality letterhead on
17 them?

18 A. They are.

19 Q. And are you familiar with these documents?

20 A. Yes, I've seen them.

21 Q. And let's turn to the one that says, is
22 marked -- dated August 19, 2004, and is in the form of a
23 letter to Mr. Jerry Abbott. Do you have that there?

24 A. I do.

25 Q. And is that marked S-2 or S-3?

1 A. It's S-2.

2 Q. In this Exhibit S-2, can you read for us the
3 first sentence of that letter, please?

4 A. Regarding or below that?

5 Q. I am writing you to notify.

6 A. Yes. Mr. Abbott, I am writing to notify you
7 that the Arizona Department of Environmental Quality is
8 suspending the approvals for sanitary facilities for
9 subdivisions for the Flagstaff Meadows Townhomes and
10 Flagstaff Meadows Unit II.

11 Q. Then could you read us the last sentence of
12 that same paragraph.

13 A. Currently, it is unclear who the water
14 supplier is for the above two listed subdivisions.

15 Q. And you're familiar with this letter; is that
16 correct?

17 A. I've seen it, yes.

18 Q. And then let's turn to Exhibit S-3, which is a
19 document that says ADEQ memorandum, and it's from Jeffrey
20 W. Stuck, safe drinking water section manager. Do you
21 have that?

22 A. I do.

23 Q. And have you seen this document before?

24 A. Yes.

25 Q. Could you turn to Page 3. And do you see that

1 there is a paragraph there that says: There are several
2 regulatory requirements/demonstrations the Flagstaff
3 Meadows subdivision (Utility Resources, L.L.C.) will need
4 to complete prior to commencing additional sales. I have
5 listed these in consecutive order?

6 A. Yes, I do.

7 Q. Then there's a list of six items; is that
8 correct?

9 A. Yes, there are.

10 Q. Have you received any formal or official
11 documentation from ADEQ since the issuance of these two
12 documents which are both dated August 19, 2004?

13 A. I have.

14 Q. Would you like to share those with us?

15 A. That was part of the, of one of the exhibits
16 that Mr. Sallquist presented. It would be Exhibit A-7.

17 Q. Could you describe Exhibit A-7?

18 A. A-7 is -- are two documents, the first of
19 which is certificate of approval of sanitary facilities
20 for subdivision, incorporating sewage collection systems.
21 And it's for Flagstaff Meadows Unit II. It was issued
22 10-8 of '04 by ADEQ. Second page is the same document for
23 Flagstaff Meadows Townhomes, issued the same date by ADEQ,
24 Arizona Department of Environmental Quality.

25 Q. And do you see on both of those documents that

1 are marked as A-7 it says water supplied by?

2 A. I do.

3 Q. And what does it say after that?

4 A. It says water supplied by Bellemont water
5 system and in parentheses PWS No. 0-300.

6 Q. Who or what is the Bellemont water system?

7 A. That is the same water system that has been in
8 existence for the truck stop. The truck stop water
9 system, that's the same identification number that it's
10 had from the time that I purchased it.

11 Q. Now, could you turn back to the memorandum
12 from Mr. Stuck, that is marked as Exhibit S-3.

13 A. Yes.

14 Q. And can you read the first sentence of the
15 first full paragraph on Page 2.

16 A. On Page 2?

17 Q. That's correct.

18 A. The first sentence of which paragraph?

19 Q. The first full paragraph.

20 A. Oh, it appears the actual water system for the
21 Flagstaff Meadows subdivision is the Bellemont Travel
22 Center, PWS ID number 03-300, a transient noncommunity
23 water system not currently under Arizona Corporation
24 commission regulation.

25 Q. Then can you go ahead and read the next

1 sentence as well?

2 A. This system will need to be reclassified from
3 the current transient noncommunity water system to
4 community water system by ADEQ in order to expand its
5 service to the Flagstaff Meadows subdivision.

6 Q. And has in fact the system been reclassified
7 to a community water system?

8 A. That's a good question. I've had that
9 conversation with Jeff Stuck. I'm not sure if it's
10 actually being reclassified, but what I've agreed to do,
11 some time ago, when this issue first came up, I agreed
12 that we would test it under the same criteria that a
13 community water system would be under. Whether it's
14 physically happened, according to ADEQ's documentation, I
15 don't know.

16 Q. So as of today, at the hearing, you have no
17 documentation from ADEQ reflecting the reclassification of
18 the Bellemont water system to a community water system; is
19 that correct?

20 A. I do not.

21 Q. And would you agree that that is something
22 that it would be appropriate to submit as a late-filed
23 exhibit to the extent that you obtain that documentation?

24 A. I would.

25 Q. And let's talk a little further about these

1 ADEQ approvals.

2 You mentioned that you've been providing
3 service up there for a while now. How did it come to pass
4 that ADEQ approved the water system up there for the
5 subdivision?

6 A. Well, it was an existing water system, so I
7 honestly don't know how it is that they did that.

8 Q. When you say, sir, it's an existing water
9 system, the truck stop water system was existing; is that
10 correct?

11 A. That's correct, yes.

12 Q. And then that water system was extended to
13 serve a residential subdivision; is that correct?

14 A. That's correct.

15 Q. And can you explain how ADEQ came to approve
16 that extension or did they ever approve it?

17 A. We submitted the -- yes, we submitted all of
18 the documentation where plans were submitted. The normal
19 forms were submitted, and they gave us an approval to
20 construct. We built them, got an engineer's certificate
21 afterwards, and got an approval of construction.

22 Q. And at anytime during this process did you
23 represent to ADEQ that approval and a certificate of
24 convenience and necessity from the Arizona Corporation
25 Commission was not necessary for this project?

1 A. No. Did I?

2 Q. Yes.

3 A. No.

4 Q. Did you or any entity under your operation or
5 control make that representation?

6 A. No.

7 Q. Are you aware of whether ADEQ would normally
8 issue such approvals without a CC&N or declaration from
9 the ACC that no CC&N is necessary?

10 A. I don't know.

11 Q. You mentioned the approval to construct and
12 approval of construction. Those were listed as, I guess,
13 exhibits to your application; is that correct?

14 A. That's correct.

15 Q. Do you recall which tab that is?

16 A. I believe 7.

17 Q. Tab 7. Would you turn to Tab 7 for us.

18 The first document I see there is certificate
19 of approval to construct water facilities. Do you see
20 that?

21 A. I do.

22 Q. And do you see the named project owner on that
23 document?

24 A. I do.

25 Q. And what is the name of the project owner?

1 A. Fuelco, Incorporated is what it says.

2 Q. It does not say Utility Source, L.L.C., does
3 it?

4 A. It does not.

5 Q. It does not say Greenfield Land Development,
6 L.L.C., does it, sir?

7 A. It does not.

8 Q. It doesn't even say Fuelco Travel Center,
9 L.L.C., does it?

10 A. No, it doesn't.

11 Q. So who is Fuelco, Inc.?

12 A. I presume that they are looking at Fuelco, who
13 is the legal owner of that property.

14 The technical name of the owner of that is
15 Fuelco Travel Center, L.L.C. It looks like they put it
16 down as Fuelco, Incorporated.

17 Q. So you're saying this official document from
18 the Department of Environmental Quality is incorrect or
19 erroneous?

20 A. I would look at it as a typo.

21 Q. Have you made any effort to correct the record
22 in that regard with the Department of Environmental
23 Quality?

24 A. I have not.

25 Q. I'm looking at a couple documents, and there's

1 another document that says certificate of approval to
2 construct drinking water facilities. Do you see that?

3 A. The document immediately after that?

4 Q. I believe there's a document in between.

5 A. It's a one-line document, Mr. Sabo. Are you
6 talking about the one-line document on the second page?

7 Q. No, there's a one-line -- a page that has one
8 line on it, and then there's another page that says
9 provisional verification.

10 A. Yes.

11 Q. And then the document after that.

12 A. The document after the provisional
13 verification?

14 Q. Right.

15 A. Yes.

16 Q. That says certificate of approval to construct
17 drinking water facilities?

18 A. Uh-huh.

19 Q. And what's the project owner listed as there?

20 A. Project owner, Greenfield Land Development,
21 L.L.C.

22 Q. It's not listed as Utility Source, L.L.C. is
23 it, sir?

24 A. It is not.

25 Q. Could you turn back briefly to Exhibit S-3,

1 the ADEQ memorandum dated August 19th, 2004?

2 A. Before we go on could I point one thing out?

3 Q. Go ahead.

4 A. The first document that we looked at that had
5 Fuelco, Incorporated, it did have the system number
6 03-300.

7 Q. That was kind of what I was going to ask you,
8 with regard to this August 19, 2004 memorandum, you see
9 there's a little chart on the first page?

10 A. I'm sorry, where are we talking about?

11 Q. Exhibit S-3.

12 A. Oh.

13 Q. Mr. Stuck's memorandum.

14 A. Okay. I've got it, yes.

15 Q. There's a chart there on the first page. Do
16 you see that?

17 A. I do.

18 Q. And they list two different PWS ID numbers,
19 public water system ID numbers. Do you see that?

20 A. I do.

21 Q. Can you explain that?

22 A. I don't, no. The first two are 03-300 -- the
23 middle one is 03-394. No, I don't.

24 Q. So that is a matter that will need to be
25 resolved again with ADEQ; is that correct?

1 A. Yes.

2 Q. And you're working on that?

3 A. We are.

4 Q. And likewise, that would be something that you
5 would agree to provide as a late-filed exhibit?

6 A. I would.

7 Q. I think we've exhausted the fun area of
8 Department of Environmental Quality.

9 Let's talk about the rates that are being --
10 you're currently charging for water service; is that
11 correct?

12 A. The homeowners association is currently
13 charging for water service, yes.

14 Q. And that would be the homeowners association
15 that you own and control?

16 A. We have control of it. We don't actually own
17 it, I guess.

18 Q. That you have control of?

19 A. We have control of it, yes.

20 Q. And how were those existing rates set, sir?

21 A. They mirror the Flagstaff rates.

22 Q. So there was no independent analysis of what
23 the appropriate rates would be for this particular
24 subdivision?

25 A. There was not.

1 Q. Likewise, were those rates in any way, shape,
2 or form approved by the Arizona Corporation Commission?

3 A. No.

4 Q. As long as you mentioned it, let's talk a
5 little bit about this wholesale arrangement, as you call
6 it, with the homeowners association.

7 By we are providing wholesale water service to
8 the homeowners association, who is the "we" in that
9 statement? Is it Utility Source, L.L.C., Greenfield Land
10 Development, L.L.C., Fuelco, L.L.C., yourself? What is
11 it?

12 A. Well, I guess Utility Source doesn't honestly
13 exist. What our intention has been, I think I mentioned
14 is that as soon as the CC&N is granted we would deed all
15 of these facilities from whatever entity holds them at
16 this point to Utility Source, L.L.C. That would be our
17 intention.

18 When I say "we," I'm speaking of Greenfield
19 Land Development providing water on a, it would be either
20 Greenfield Land Development or Fuelco would be providing
21 water to the homeowners association on a wholesale basis,
22 then the homeowners association is billing and has billed
23 to the individual customers on a monthly basis for their
24 individual use.

25 Q. So the wholesale provider to the homeowners

1 association, as you characterize it, is both Greenfield
2 and Fuelco Travel Center, L.L.C.?

3 A. It probably would be more accurate to say
4 Fuelco.

5 Q. You mentioned some of the facilities are owned
6 by Greenfield; correct?

7 A. That's correct.

8 Q. So --

9 A. It would be a combination of the two, that's
10 correct.

11 Q. Is there a formal arrangement or contract
12 between Fuelco and Greenfield with regard to the provision
13 of this wholesale service?

14 A. Part of the homeowners association documents,
15 they deal directly with this.

16 Q. I asked you, sir, about any written agreement
17 between Greenfield and Fuelco. Is there such a document?

18 A. Between Greenfield and Fuelco?

19 Q. That's correct.

20 A. Between those two entities?

21 Q. That's correct.

22 A. I don't believe so.

23 Q. And you kind of anticipated my next question,
24 which was: Is there any contract between either
25 Greenfield or Fuelco or both and the homeowners

1 association?

2 A. Through the homeowners association documents,
3 yes, sir.

4 Q. Is Greenfield a party to those documents?

5 A. I would have to go back and review them. I
6 believe they are, but I'd have to go back and review it
7 again.

8 Q. By documents, you mean like the CC&Rs or...

9 A. The CC&Rs, and -- yes, the CC&Rs.

10 Q. In this wholesale arrangement, was that
11 arrangement approved by the Arizona Corporation
12 Commission?

13 A. No, it was not.

14 Q. Are you aware of any authority or any prior
15 circumstance where a similar situation was found to be
16 valid or appropriate by this Commission?

17 A. No.

18 Q. How did you come to the idea that a wholesale,
19 as you call it, a wholesale provision of service between
20 one or two entities that you control and another entity
21 that you control, that that arrangement would enable you
22 to evade regulation by this Commission?

23 A. It has never been the intention of myself or
24 any other entity that I'm associated with to evade
25 anything. I did not have the understanding that I was

1 supposed to be regulated by the Corporation Commission.

2 Q. How did you come to that conclusion that you
3 were not supposed to be regulated?

4 A. I've never dealt with the Corporation
5 Commission in any of my dealings in developing anything
6 that I've ever dealt with before. I've never dealt with
7 the Corporation Commission.

8 Q. Did you look into the matter at all?

9 A. Did I call up the Corporation Commission and
10 ask them, no. What I did is I took all of the approval
11 documents, which are required in order to record a final
12 plat, which are the Coconino County documents, the
13 Department of Real Estate documents, and we fulfilled
14 those requirements.

15 Q. I just wanted to make sure you're not
16 asserting or relying on some sort of legal opinion that
17 was provided to you at that time as a defense.

18 A. No, I'm not.

19 Q. And you've mentioned, when Mr. Sallquist was
20 questioning you, you mentioned various positions that
21 different agencies such as ADEQ, the Department of Real
22 Estate, the Department of Water Quality, that those
23 agencies have taken. You're not authorized to speak on
24 behalf of any of those agencies, are you, sir?

25 A. Not to my knowledge, no.

1 Q. That means no, okay, good.

2 You would agree with me that the climate of
3 this state is characterized by a desert, or at the very
4 best, semi desert or arid climate?

5 A. I would.

6 Q. And you're also aware that this state is
7 facing a very severe drought?

8 A. I am very aware of that.

9 Q. That's had a lot of impacts throughout the
10 state; isn't that right?

11 A. Yes.

12 Q. And you certainly would agree that that is a
13 matter that we should all be concerned with; right?

14 A. Yes, I would.

15 Q. And that it's important for the Commission, as
16 a body that regulates water service, to keep that foremost
17 in its mind?

18 A. Yes.

19 Q. Along those lines, then, the proposed
20 development that we're talking about here, is there any
21 type of lake or pond that is associated with the
22 development?

23 A. There is.

24 Q. Can you describe that for us?

25 A. I can. There is a lake somewhere close to the

1 middle of the project which serves as a detention lake,
2 and it also serves as a water feature for the area.

3 Q. Is that on the map?

4 A. It's not -- if you look at this drainage
5 channel right in here, there is a park in the middle of it
6 right here, and there is a lake right here and then a
7 water feature that goes down here, and connects to the
8 sewer treatment plant.

9 Q. Describe this water feature that you just
10 mentioned.

11 A. It is something that I think is very
12 attractive. It is a lake, about an acre, I think about an
13 acre lake. It is, has some waterfalls in it, that sort of
14 thing, and it has a creek that runs down into another
15 small holding pond. And basically, it's just, it's an
16 attractive water feature, in our view. We've utilized
17 reclaimed water to fill that with, and we feel like it's a
18 good use of reclaimed water. And we also irrigate out of
19 that, utilizing reclaimed water for the common areas.

20 Q. So the water for this lake and creek and
21 retaining pond, does it come from the wastewater treatment
22 plant?

23 A. It does.

24 Q. And is this lake permitted as a groundwater
25 recharge facility?

1 A. It is not. Would we like it to be? Yes.

2 Q. Are you working on that?

3 A. We are working on that.

4 Q. But it's not currently?

5 A. It is not. That's one of the things that we
6 hope to do as part of our plan for Phase III. We want to
7 do everything we can to utilize the water we've got there,
8 and that's one of the things that HydroSystems is going to
9 be working on, is a recharge permit.

10 Q. I'll throw this question out. If you're not
11 competent to answer or you think it would be better for
12 your hydrologist to answer, go ahead and tell me.

13 A. Okay.

14 Q. I guess my understanding is sort of the
15 aesthetic characteristics of a water body may work against
16 the characteristics that are favorable for recharge; is
17 that correct?

18 A. I don't think so. I've looked at several
19 recharge lakes and there's some very attractive ones that
20 are done. It can be done so that it looks very, very
21 nice. And that would be our goal in developing Phase III,
22 so that it is a very attractive water feature and that any
23 excess water that we've got, instead of putting it down a
24 channel and utilizing in our NPDES, permit which took us
25 years to get, that we use this recharge and put it back in

1 the ground where it belongs, and that's in the underground
2 aquifer.

3 Q. Let's talk about that park you mentioned.
4 That's above the lake, as I understand it?

5 A. Yes.

6 Q. Is there any other turf or grass in this park?

7 A. There is.

8 Q. How is that irrigated?

9 A. It's irrigated with reclaimed water out of
10 that lake. That lake acts as a holding pond then we pump
11 out of it to irrigate it. And the other common areas that
12 are drip irrigation, we also utilize that.

13 Q. You mentioned other common areas. Do these
14 other common areas also have turf or grass?

15 A. Some of them have turf. Most of them that we
16 put in are mostly drip systems.

17 Q. Was there consideration of making this park
18 and the turf common areas that you are describing, did you
19 give consideration to having those be more of a xeriscape
20 or desert landscaping?

21 A. What our intent was that as we look at
22 individuals that move in there, you know, everyone wants
23 to have their children go to a place where they can throw
24 a football or whatever, and our intent was that if we're
25 going to have a grassy area, we wanted to have it

1 somewhere that was using reclaimed water to irrigate it
2 with, instead of individuals doing it on their own. So
3 that was the thinking as we put that together.

4 Q. And let's flip over to another topic. When
5 Mr. Sallquist was questioning you, he mentioned various
6 letters that went back and forth between him and myself;
7 is that correct?

8 A. Yes.

9 Q. You're familiar with those letters?

10 A. Yes.

11 Q. He mentioned a March 22nd, 2004 letter; is
12 that correct?

13 A. Yes.

14 Q. And that was a letter where I basically, it
15 was a demand letter saying hey, stop hooking up new
16 customers.

17 A. I remember that distinctly.

18 Q. I thought that you might.

19 And then there were various follow-up letters
20 after that.

21 A. There were.

22 Q. And the most recent of these letters is a
23 letter dated September 15, 2004; is that correct?

24 A. Yes.

25 Q. And that's a letter from myself to

1 Mr. Sallquist; is that right?

2 A. Yes, it is.

3 Q. And that's a letter concerning who counts as
4 an existing customer for the purpose of the earlier
5 letters?

6 A. That's correct.

7 Q. And that's based on an agreement between Staff
8 and Utility Source?

9 A. That's correct. And we appreciated it, by the
10 way.

11 Q. And there's a chart that's attached to that
12 letter; is that correct?

13 A. I don't have it in front of me, but I recall.
14 MR. SALLQUIST: I have extra copies, if you'd
15 like, Mr. Sabo.

16 ALJ POPE: Can I have one Mr. Sallquist?

17 MR. SABO: Sure. I don't know if we want to
18 mark that one or not.

19 MR. SALLQUIST: I have the March 22nd letter,
20 too.

21 Q. BY MR. SABO: Going back, then, to my
22 September letter, attached to that is a chart. Do you
23 have that in front of you?

24 A. I do.

25 Q. That was a chart that was provided by your

1 counsel, Mr. Sallquist?

2 A. That's correct.

3 Q. And that says customers as of March 22, 2004;
4 is that correct?

5 A. Yes, it is.

6 Q. Is that an accurate representation of the
7 customers as of March 22nd, 2004?

8 A. Yes.

9 Q. And it lists 201 lots there; is that correct?

10 A. That's correct.

11 Q. And you have agreed, until such time as the
12 Commission issues a certificate of convenience and
13 necessity, that you will provide service to those 201
14 lots, and nobody else?

15 A. We will.

16 Q. And by "we," you're talking about Utility
17 Source, Greenfield Land Development, L.L.C., Fuelco, Inc.,
18 Fuelco, L.L.C., yourself, your associate, Mr. Bulechek,
19 and so forth?

20 A. Yes, we will.

21 Q. You mentioned you're an experienced
22 businessman; right?

23 A. Well --

24 Q. You've been retired for a while?

25 A. Based on this, I'm sort of questioning that,

1 but yes, I'll try.

2 Q. As an experienced businessman, you believe
3 it's important to stand by your word; right?

4 A. I do believe that.

5 Q. And to back your customers up?

6 A. I do believe that.

7 Q. And I wanted to make sure for the record,
8 then, that yourself and these entities that you control
9 are going to stand behind Utility Source, L.L.C.?

10 A. We will.

11 Q. Because a concern that we may have is by
12 putting it off in a separate L.L.C. that you might walk
13 away from that. But you're not going to do that?

14 A. That is not our intent.

15 Q. And you're committing not to do that?

16 A. Say it again.

17 Q. Are you committing today for the record not to
18 do that? Not to walk away and let it fail?

19 A. We will not let it fail. Mr. Sabo, I'm
20 building my own home in there, and I've got a couple of
21 kids living in there, too, so that is not going to happen.

22 Q. We've run into that situation before where a
23 developer has a water company and walks away from it, so
24 we wanted to be very careful that that will not happen in
25 this situation.

1 A. We appreciate that.

2 Q. And as I'm sure you've come to learn to your
3 possible dismay, there are numerous statutes and
4 regulations that govern a public service corporation.

5 A. Well, I would say that I'm a lot more familiar
6 with it today than I have been, yes.

7 Q. And it's your intent to in fact comply with
8 all these requirements?

9 A. It is.

10 Q. And you're going to use your best efforts to
11 do so?

12 A. I will.

13 Q. And to retain appropriate and experienced
14 personnel who are familiar with these requirements, and
15 can ensure that you comply with them?

16 A. I will.

17 Q. Well, I almost hesitated to ask this question.

18 A. Then don't.

19 Q. I think we should be clear for the record in
20 terms of what areas are being covered in what
21 Mr. Sallquist calls Phase I versus Phase II, or as I would
22 put it, what areas are included in the DWR letter that is
23 marked as Exhibit A-10. So can you run through that one
24 more time using the map.

25 A. We would include everything in the green that

1 is marked Utility Source, Bellemont truck stop,
2 undeveloped, and Microtel motel.

3 ALJ POPE: Could I ask that you list them each
4 one by one. I mean, just for my purposes, because I can't
5 see it from here.

6 THE WITNESS: Utility Source, Bellemont truck
7 stop, undeveloped, and Microtel motel.

8 The Bellemont fire station, Flagstaff
9 Meadows II, Flagstaff Meadows I, and the townhomes of
10 Flagstaff Meadows, and the sewer treatment plant.

11 Q. BY MR. SABO: Those are all included in the
12 DWR letter; is that correct?

13 A. That's correct.

14 Q. And so what areas are not included in the DWR
15 letter?

16 A. The area that is not included would be what
17 we're calling here Flagstaff Meadows III, and Flagstaff
18 Meadows -- I'm sorry, the townhomes at Flagstaff
19 Meadows II, and then the Bellemont commercial.

20 Q. And again, just so that we're clear for the
21 record, Exhibit A-6, the legal description, which part of
22 that is included in the DWR letter and which part is not?

23 A. If you took the first page of Exhibit A-6 and
24 combine that with the second page, that would be the area
25 that would be included.

1 Q. So page --

2 A. That would cover the ADWR letter.

3 Q. Page 1 and Page 2?

4 A. Page 1 and Page 2, so that we make sure we've
5 got it straight on top of it, it would be the one that
6 says legal description, and Utility Source, and then the
7 next one would say legal description and Flagstaff Meadows
8 I and II.

9 Q. And then the last page would be the area not
10 covered by the DWR letter?

11 A. That is not correct. The last one is
12 everything.

13 Q. Okay, so if you took Page 3, and subtracted
14 out Page 1 and Page 2?

15 A. You would have, that's correct, right. Page 3
16 is the entire parcel on the map.

17 MR. SALLQUIST: Mr. Sabo, I hate to interrupt,
18 but to clarify.

19 MR. SABO: Go ahead.

20 MR. SALLQUIST: Does that include the Utility
21 Source, the green area?

22 THE WITNESS: It does.

23 MR. SALLQUIST: I was under the impression it
24 excluded it. Sorry to interrupt.

25 Q. BY MR. SABO: Going back to the exciting green

1 area, there is --

2 A. You're right, excuse me, I'm sorry, he's
3 correct.

4 MR. SALLQUIST: The entitlements doesn't
5 indicate that it includes that area.

6 THE WITNESS: That's correct. What we would
7 have to do when it includes all three of them, you would
8 take then Page 1 and Page 3, and put those together, and
9 that would be the entire parcel. So what I would envision
10 that we would do is we would put these legal descriptions,
11 and it would just say and, and then put them together.

12 Q. BY MR. SABO: So Page 3 is the area not
13 covered by the DWR letter? Or you lost me, I'm sorry.

14 MR. SALLQUIST: I think, Your Honor, Mr. Sabo,
15 the parcels that are identified on A-5 in the very fine
16 print in the colored areas are listed at the tops of the
17 legal pages. I think they're distinct areas there.

18 The third page is everything -- why the
19 engineer did this, we will never know -- but the third
20 page is the entire area that you see on Exhibit A-5,
21 excluding that in the northwest corner, that green area.
22 So Page 3 does include parcels -- portions of Phase I and
23 all of Phase II.

24 THE WITNESS: If you put Page 1 and Page 3
25 together, it's everything.

1 MR. SALLQUIST: There's no overlap. Page 1
2 and Page 3 are exactly that. But I think what Mr. McCleve
3 is testifying is Page 1 and Page 2 are the 325 lots that
4 are in the PAD.

5 THE WITNESS: Right.

6 Q. BY MR. SALLQUIST: Okay. And that's an
7 excellent clarification, because that was going to be my
8 next question, to clarify the, what Mr. Sallquist calls
9 Phase I or the area covered by the DWR letter that is
10 marked Exhibit A-10. How many lots are in that area?

11 A. The area that is not included in the letter.

12 Q. In the letter?

13 A. Oh, in the letter there's 325 residential
14 lots.

15 Q. And how many, then, lots are not included in
16 the DWR letter?

17 A. 350.

18 Q. The 201 lots that are listed in the attachment
19 to my September letter, are all of those 200 lots included
20 in the 325 lots that you mentioned, are included in the
21 DWR letter area?

22 A. They are.

23 ALJ POPE: While they take a minute, I have a
24 question really quickly. You listed the Townhomes II and
25 Bellemont commercial as not being included in the ADWR

1 letter.

2 THE WITNESS: The townhomes at Flagstaff
3 Meadows II is not, and Flagstaff Meadows III is not, and
4 the Bellemont commercial is not.

5 ALJ POPE: And that comprises Phase II?

6 THE WITNESS: It actually -- yes, the way
7 you're looking at it, it's Phase II.

8 ALJ POPE: Thank you. I'm sorry.

9 MR. SABO: Thank you, Your Honor.

10 Q. BY MR. SALLQUIST: Mr. McCleve, the area
11 included in the DWR letter, that includes the area at the
12 upper left-hand corner of the map that's marked Utility
13 Source; is that right?

14 A. Yes, it does.

15 Q. And what is that area?

16 A. That area right now is all wells. That's
17 where our wells and that's where our water system is.
18 That's where our storage tanks, all of the facilities to
19 do with the backbone of the water system is located on
20 that site.

21 Q. So you're not requesting authority to put any
22 residential hookups in that area?

23 A. We are not. Our long-term intent is to build
24 an RV park there, but we understand that the day that we
25 do that, we would have to get Department of Water

1 Resources approval for water adequacy, and we're aware of
2 that.

3 Q. And likewise, then, you would also agree that
4 you'd have to come back for an expanded CC&N to serve any
5 customers or RV park in that area?

6 A. We are aware of that.

7 MR. SALLQUIST: Your Honor, it was my
8 understanding that the entire green area that includes
9 those four designated parcels are, in fact, included in
10 what we're calling Phase I, the certificate that
11 encompasses the 325 lots in the PAD letter. So it could
12 be developed. It would have to require -- meet all of the
13 requirements of the other agencies, but it would have a
14 CC&N that would permit future development of the parcel
15 that's labeled Utility Source.

16 MR. SABO: I guess we're having a difference,
17 then, in understanding as to that Staff's intent, I
18 believe, is to only recommend approval of areas where
19 there is going to be a PAD issued for the area. And
20 since, as I understand it, there will be required an
21 additional PAD for this RV park, then that type of RV park
22 service will not be included in the CC&N that we are
23 recommending.

24 MR. SALLQUIST: Your Honor, perhaps we should
25 have the hydrologist clarify what requirement might be for

1 a PAD. I was under the impression the PAD covered all of
2 that green area.

3 ALJ POPE: That's what the understanding is
4 that I was going on. Perhaps we could have some
5 clarification on that.

6 MR. SABO: Likewise, Your Honor, might be
7 Mr. McCleve knows this, and if not, we can move it onto
8 the hydrologist.

9 Q. BY MR. SABO: But there's an area marked
10 undeveloped there, and what is that area?

11 A. It's property that I own, that is zoned
12 commercial. We don't have any specific plans for it in
13 the future. We don't have any immediate plans for it but
14 some day I would anticipate that it would be developed.

15 Q. Are you asking that this area be included in
16 the so-called Phase I CC&N?

17 A. Yes, the area. But our intent, again, if we
18 add additional units, my understanding of it is that we
19 add additional units, we have to prove that we've got the
20 water to serve that.

21 Q. Your understanding, then, it would be that at
22 this time or the PAD that DWR is contemplating issuing
23 does not include development on that area marked
24 undeveloped?

25 A. Yes.

1 Q. Or you don't know?

2 A. I don't know whether they've specifically even
3 dealt with that. They probably haven't even dealt with
4 that.

5 Q. Mr. McCleve, are you aware of any prior orders
6 by this Commission approving a hookup fee for an initial
7 CC&N application?

8 A. I am not familiar with any of your orders.

9 Q. Likewise, then, you're not familiar with any
10 orders approving a financing under a situation similar to
11 this?

12 A. No.

13 Q. Sticking with the hookup fee for a minute, you
14 mentioned additional infrastructure. Can you clarify for
15 me what -- I thought that all the infrastructure was in,
16 yet apparently that's not correct. So what would be left
17 to build?

18 A. Most of the infrastructure is in.
19 Potentially, well sites, recharge system, additional
20 lakes. We possibly would have to enlarge our sewer
21 treatment plant at the full buildout of what we've got
22 anticipated there. Those are the things that we'd be
23 talking about for future, you know, as additional units
24 and as additional flows come on, in order to accommodate
25 those flows.

1 Q. And has Greenfield Land Development, L.L.C.,
2 Fuelco Travel Center, L.L.C., Empire Development, L.L.C.,
3 Flagstaff Meadows, L.L.C., or Greenfield Land Development
4 pension plan, have any of those entities entered into a
5 main extension agreement with regard to any of the areas
6 described on the map?

7 A. A main extension agreement, what does that
8 mean? I'm not clear.

9 Q. Are you familiar with what a main extension
10 agreement is?

11 A. Could you clarify what you're meaning? You
12 mean to other properties outside of this property?

13 Q. No, sir. A main extension agreement is a
14 specific type of agreement contemplated by our rules. I
15 take it you're not familiar with that?

16 A. Apparently not.

17 MR. SALLQUIST: If it clarifies the record,
18 Mr. Sabo, I can tell you that we have not prepared those
19 at this point.

20 MR. SABO: Thank you.

21 THE WITNESS: Sorry.

22 Q. BY MR. SABO: Now, you mentioned the assets in
23 the -- that would be used to provide water service, and
24 you've explained now the ownership of those assets is not
25 currently with Utility Source, L.L.C.; is that correct?

1 A. That's correct.

2 Q. And your proposal is once a CC&N is granted,
3 that these assets then would be transferred to Utility
4 Source, L.L.C.; is that correct?

5 A. That is correct.

6 Q. Are you or the entities you are affiliated
7 with expecting any consideration or payment for these
8 assets from Utility Source, L.L.C.?

9 A. No.

10 Q. And exactly when are you contemplating
11 transferring the assets? The first time the Commission
12 issues an order granting any CC&N for any part of this
13 area, would that be what causes it?

14 A. If the Corporation Commission directed us to
15 do it prior to the actual -- whatever the Corporation
16 Commission were comfortable with, we would certainly do
17 that.

18 Q. Let's turn to the line of credit that you're
19 requesting. Is it true that the line of credit is through
20 the year 2014?

21 A. Yes.

22 Q. It's not short-term credit then, is it?

23 A. Well, when we put this together, I think our
24 intent was that it was. Maybe it isn't structured the way
25 that you like it, but we would be open to shortening that

1 up, if it were necessary.

2 Q. Currently, to answer my question, then, it is
3 not short-term credit?

4 A. No.

5 Q. And the arrangements that you have proposed
6 would be through the year 2014, there would be payments
7 only of interest and no principal payments; is that your
8 proposal?

9 A. I think that's what the documentation says.
10 The intent of that is that it would be used on a short, I
11 think I've said that we'd use it on a shortfall basis, and
12 we pay it as quickly as the funds were available to do
13 that.

14 Q. But the loan documentation that would govern
15 this would not require any principal repayments through
16 the year 2014; is that correct?

17 A. The way that it's currently structured, that's
18 correct.

19 Q. Again, under the governing loan documents that
20 you're proposing, regardless of what your intent is, under
21 those governing loan documents, it would be allowed to use
22 loan proceeds for operating expenses?

23 A. Yes.

24 Q. Is basically what you're trying to use this
25 line of credit for is for working capital for the Utility

1 Source, is that fair to say, or would you give it a
2 different characterization?

3 A. That's probably a good description.

4 Q. And you mentioned the need for any such loan
5 would be less if Staff's proposed rates were approved; is
6 that correct?

7 A. Yes, it is.

8 Q. And you mentioned you'd be willing to resize
9 the cross connection or backflow prevention tariff and the
10 curtailment plan tariff to reflect the types of tariffs
11 that are currently recommended by Staff for those areas?

12 A. Yes, we would.

13 Q. And you mentioned you've got an employee out
14 there running this thing?

15 A. Yes. We've got an employee that is on
16 Greenfield Land Development payroll, but we have a
17 certified operator that's under contract.

18 Q. Let's deal with them one by one. Who is this
19 employee?

20 A. Jeremy McCaleb.

21 Q. What kind of experience does he have in
22 running a water system?

23 A. Probably limited. He works at the direction
24 of our operator.

25 Q. So in and of himself, he's not certified or

1 qualified to operate the system?

2 A. He is not. I think that's his intent, is to
3 learn that. And he doesn't have a great deal of
4 knowledge, no.

5 Q. And is it the plan, then, that once Utility
6 Source, L.L.C. gets going and is granted the L.L.C., that
7 will this individual be employed by Utility Source?

8 A. We haven't addressed that at this point. Our
9 intent is to have the certified operator, we would utilize
10 him primarily to give direction to how it's operated, and
11 that employee would be at his beck and call, basically, as
12 he is needed.

13 Q. Who would he be working for, then?

14 A. He would be working at the direction of
15 A Quality Water, Pat Carpenter, who is the certified
16 operator.

17 Q. Where would the checks be coming from?

18 A. That's a good question. We would probably,
19 because he works right now for Greenfield Land
20 Development, he would probably be working on a contract
21 basis for Utility Source, because we don't need him all
22 the time there, under Utility Source, so he wouldn't be a
23 full-time employee of Utility Source.

24 Q. In other words, so would there be a contract,
25 then, between Greenfield and Utility Source to provide for

1 his services on a part-time basis?

2 A. There would be.

3 Q. I see. And then you mentioned the certified
4 operator. Who is that?

5 A. Pat Carpenter, A Quality Water.

6 Q. Is it the individual or the entity that is the
7 certified operator, technically, if you know?

8 A. I'm not sure.

9 Q. And in any event, you're using the certified
10 operator to meet the regulatory requirements of DEQ?

11 A. We are.

12 Q. And you intend at all times to maintain a
13 certified operator to operate this system?

14 A. We will.

15 Q. Do you have a contract in place with the
16 certified operator?

17 A. We do.

18 Q. Is that a contract with Greenfield Land
19 Development, L.L.C.?

20 A. Yes.

21 Q. And how would Utility Source fit into that
22 contract?

23 A. We would name Utility Source -- we would
24 nominate Utility Source in our place, because he would
25 work directly for Utility Source.

1 Q. Could you turn back to Exhibit A-10, the
2 status letter from ADWR.

3 A. Yes, I have it.

4 Q. And do you see the second paragraph there?

5 A. Yes.

6 Q. And they mentioned Flagstaff Meadows Unit I,
7 and in parentheses it says 133 lots. Do you see that?

8 A. I do.

9 Q. And then Flagstaff Meadows Unit II, and then
10 in parentheses it says 87 lots?

11 A. Yes.

12 Q. And then it says townhomes at Flagstaff
13 Meadows Unit I?

14 A. Yes.

15 Q. In parentheses it says 105 lots?

16 A. I do.

17 Q. Then it says for a total of 325 dwelling
18 units?

19 A. Yes.

20 Q. That doesn't contemplate, then, any dwelling
21 units attributable to an RV park or to development in the
22 parcel marked undeveloped?

23 A. It does not.

24 MR. SABO: Your Honor, on a procedural note, I
25 would note that Mr. Fisher, due to other requirements, has

1 to leave at 4:30, so maybe we could take him out of order.

2 ALJ POPE: Okay.

3 Do you have any objection to that,

4 Mr. Sallquist?

5 MR. SALLQUIST: We have no objection to that.

6 ALJ POPE: We'll have him next.

7 MR. SABO: That was the end of my

8 cross-examination.

9 ALJ POPE: Did you have any redirect,

10 Mr. Sallquist?

11 MR. SALLQUIST: I think just one area, Your

12 Honor.

13

14

REDIRECT EXAMINATION

15 BY MR. SALLQUIST:

16 Q. Mr. McCleve, if you'd refer to Exhibit A-2,
17 the financing application, and going about five or six
18 pages to Attachment A, Page 2 of 5. I beg your pardon,
19 I'm on the wrong page. It's page four of five. It's a
20 couple more pages past that one, called the pro forma cash
21 flow.

22 A. Yes, I have that one.

23 Q. Looking at the first column, 2005, if you'll
24 go down about halfway, you'll find a line indicating
25 working capital loan. Do you find that line?

1 A. Yes, I do.

2 Q. That indicates that the company will need
3 \$575,000 basically to end up with a zero net cash flow on
4 the very bottom line; correct?

5 A. Yes.

6 Q. It shows 995, but for all practical purposes
7 it's zero?

8 A. Right.

9 Q. Those are the cash requirements for the
10 operating expenses and the capital requirements of the
11 company in that first year of operation; correct?

12 A. That's correct.

13 Q. Now, if you'll go down, probably
14 three-quarters of the way down, under uses of cash, it
15 says working capital repayment.

16 A. Yes.

17 Q. If you go over into year three, four and five.

18 A. Yes.

19 Q. Does that start to show that the company is in
20 fact repaying a portion of the principal balance?

21 A. It does.

22 Q. I think you testified earlier that with the
23 Commission Staff recommended rates, you probably would
24 have more disposable income than you would under your
25 proposed rates; right?

1 A. Yes. And our intent would be to pay it down
2 as quickly as we can.

3 Q. So you might be able to pay it back sooner and
4 in larger amounts than originally contemplated in your
5 application; correct?

6 A. That's right.

7 Q. That does not do away with the need to have
8 that working capital early on in the operation of the
9 company, does it?

10 A. No, it doesn't.

11 Q. Again, it would be hopeful that that would be
12 paid off long before the 2014 promissory note that is
13 associated with that working capital?

14 A. I certainly hope so.

15 Q. And you wouldn't have any objection of the
16 Commission shortening the term of that revolving line?

17 A. No, we would not.

18 Q. But it's still the company's position that
19 they need to have a revolving line to take care of cash
20 needs?

21 A. Yes.

22 Q. You had said in answer to a question by
23 Mr. Sabo that you're going to convey these facilities to
24 the utility company without consideration. You would
25 receive, in exchange for that, the membership interest or

1 the membership equity of the company, would you not?

2 A. Yes, that's correct.

3 Q. So that would actually be an investment by
4 whoever the present owners of those assets are in Utility
5 Source in exchange for the assets?

6 A. That's correct.

7 Q. So it is an investment, it's not a
8 contribution to the utility company?

9 A. That's correct.

10 Q. Mr. Sabo also quizzed you on a number of the
11 ADEQ approvals to construct or approvals of construction
12 and the names of the entities. Who submits those
13 applications to ADEQ for AOCs? Is that the company or is
14 it the --

15 A. It's my engineer.

16 Q. So it's the engineering company or the
17 contractor that would submit them?

18 A. Right.

19 Q. Is it conceivable that he may not know the
20 exact name of the entity that owns them?

21 A. Very conceivable.

22 Q. And you think that that is perhaps a basis for
23 the reason of the diversity in the applications?

24 A. I do.

25 Q. And you, I think, testified that you do not

1 know how that one strange PWS number got in there, do you?

2 A. I have no idea how that got in.

3 Q. Do you know whose number that is?

4 A. I don't.

5 MR. SALLQUIST: I think the other things I
6 wanted to clarify, Your Honor, would be with the
7 hydrologist, so I would have no further redirect of
8 Mr. McCleve.

9 ALJ POPE: Thank you.

10 MR. SABO: May I have recross?

11 ALJ POPE: Sorry.

12 MR. SABO: Thank you, Your Honor. I
13 appreciate the indulgence.

14

15 RE CROSS-EXAMINATION

16 BY MR. SABO:

17 Q. Mr. McCleve, Mr. Sallquist on redirect asked
18 you some questions about the transfer of assets from the
19 existing owners to Utility Source, L.L.C.

20 A. Yes.

21 Q. And you mentioned that in exchange for those
22 assets, the owners of the assets would get equity interest
23 in Utility Source, L.L.C.?

24 A. That's correct.

25 Q. Now, I thought that you had previously

1 testified that you already owned 80 percent of Utility
2 Source, L.L.C. and the other 20 percent was owned by your
3 colleague, Mr. Bulechek; is that correct?

4 A. That is correct. I guess the discrepancy
5 might be that we own 80 percent and 20 percent of a L.L.C.
6 that really doesn't have any assets. Once we make those
7 contributions or investments, then we would own 80 percent
8 and 20 percent of the L.L.C. that has some significant
9 assets.

10 Q. Right. So there would not be any new issuance
11 of equity made by the L.L.C., though, at that time; is
12 that correct?

13 A. No.

14 Q. There's like no membership certificates or
15 anything of that nature issued?

16 A. I would own -- I mean, we would still own our
17 pro rata share of the corporation.

18 Q. And that would not change with the asset
19 transfer?

20 A. No, we don't anticipate that change.

21 MR. SABO: Thanks for clarifying that.

22 Your Honor, that concludes my recross, and I
23 would, before Mr. McCleve gets off the stand, like to move
24 Exhibits S-2 and S-3, those two documents from DWR.

25 MR. SALLQUIST: No objection; Your Honor.

1 ALJ POPE: S-2 and S-3 are admitted.

2 You had nothing further?

3 MR. SALLQUIST: No, thank you, Your Honor.

4 ALJ POPE: Thank you.

5 (The witness was excused.)

6 ALJ POPE: Mr. Sabo.

7 MR. SABO: With your indulgence, and we thank
8 you for that, out of order, we will call Mr. Fisher at
9 this time. For some hopefully very speedy testimony.

10

11

JIM FISHER,

12 called as a witness, having been first duly sworn by the
13 Certified Court Reporter to speak the truth and nothing
14 but the truth, was examined and testified as follows:

15

16

DIRECT EXAMINATION

17 BY MR. SABO:

18 Q. Good afternoon, Mr. Fisher.

19 A. Good afternoon, Mr. Sabo.

20 Q. Can you state your name and business address
21 for the record?

22 A. My name is Jim Fisher. My business address is
23 Arizona Corporation Commission, Utilities Division, 1200
24 West Washington, Phoenix, Arizona.

25 Q. And by whom are you employed and in what

1 capacity?

2 A. I'm employed by the Utilities Division of the
3 Arizona Corporation Commission as an executive consultant,
4 primarily focused on the licensing of water utilities and
5 wastewater utilities in the form of certificates of
6 convenience and necessity. I also do technical writing
7 and coordinate Staff's position and policy recommendations
8 for hearings.

9 Q. And as part of your duties in that position,
10 were you assigned to work on this case?

11 A. Yes, sir, I was.

12 Q. And you have many years of experience here at
13 the Commission; is that correct?

14 A. Some would argue too many.

15 Q. No comment on that.

16 Did you prepare the Staff report which is
17 marked as Exhibit S-1 in this proceeding.

18 A. Yes, sir. S-1 is a September 22, 2004 Staff
19 report for the Utility Source, L.L.C. application for a
20 certificate of convenience and necessity to provide water
21 and wastewater service to a portion of Coconino County.

22 This Staff report was prepared by myself in
23 conjunction with Mr. Johnson and Mr. Chelus, as well as
24 some administrative help and the mapping capabilities of
25 Ms. Barb Wells. Unfortunately, due to the legal

1 description problems that's already been discussed,
2 Ms. Wells was unable to accomplish all of her tasks.

3 Q. So Exhibit S-1 was prepared by you or under
4 your direction?

5 A. Yes.

6 Q. And Staff is modifying its recommendations as
7 set forth in Exhibit S-1, that modification will be as set
8 forth in my opening statement today; is that correct?

9 A. Yes. It essentially -- we're trying to
10 bifurcate or trying to cut in portions the property that's
11 being sought to be entitled, and Department of Water
12 Resources has indicated that a portion of the property is
13 in most likelihood going to have a physical demonstration
14 of available water to serve 325 lots.

15 As I've read the letter, those portions are
16 included in Flagstaff Meadows I, the townhomes, and
17 Flagstaff Meadows II. Once we see that they in fact
18 obtain that physical availability demonstration
19 determination from Arizona Department of Water Resources,
20 Staff would recommend that they obtain a conditional CC&N,
21 in the event that they are able to provide that PAD in a
22 timely basis.

23 If they are not able to provide that PAD prior
24 to consideration by the Commission, Staff would recommend
25 that the initial served area and the proposed served area

1 both receive a preliminary order per the statute.

2 Q. And the area which you are saying should get
3 a -- that Staff would recommend a CC&N for that area is
4 the area specifically described in the ADWR letter that's
5 marked A-10?

6 A. I don't believe so. I believe that the DWR
7 letter refers to a number of properties. It does not nail
8 it down. The paragraph does refer to other areas, and it
9 also refers to some understanding between the developer
10 and DWR. Until such time as the area is specifically
11 described and a legal description is provided as agreed to
12 by DWR, and Commission Staff and the developer, I'm not
13 sure what we agree on on that aspect.

14 In the developer's testimony, Mr. Sabo, he
15 included a number of properties that have yet to be
16 platted. No amount of demand associated with that
17 property can be included and utilized for analysis on the
18 physical availability. Physical availability by
19 Department of Water Resources, from what I understand, in
20 reviewing our materials, is a mathematical equation. To
21 the extent that that demand has not been nailed down, we
22 will need additional clarity from Department of Water
23 Resources.

24 Q. Let me see if I've got this, then. The letter
25 describes 325 specific lots; is that correct?

1 A. Yes, sir, it does.

2 Q. So Staff would recommend approval of a
3 conditional CC&N for those 325 lots if a PAD is submitted
4 for those 325 lots?

5 A. Yes.

6 Q. And not for any other areas that the developer
7 may have described?

8 A. Correct.

9 Q. And then for the remaining areas, Staff would
10 recommend a order preliminary to a CC&N?

11 A. Yes. The Staff has issued or made a number of
12 recommendations for conditional CC&Ns. We don't believe
13 that that is appropriate at this time or the way this
14 thing has been formed. If we were to issue our
15 recommendation, rather than being the denial that's
16 included in the report, would be that it would be an order
17 preliminary in that once the applicant has provided the
18 documentation required, the Commission could then issue a
19 finding that the conditions had been met and a CC&N could
20 then be issued.

21 Q. Mr. Fisher, except as modified by your
22 testimony here today, do you adopt Exhibit S-1 as part of
23 your testimony today?

24 A. Yes, sir, I do.

25 Q. Other than the modifications that you've

1 already noted, do you have any modifications to make to
2 Exhibit S-1?

3 A. To the extent that the applicant has already
4 testified that the assets would be conveyed prior to any
5 order from the Commission, Staff would like to ensure that
6 the assets are held by the utility. We're seeking to
7 certificate an entity that is technically and financially
8 capable. Without any assets it's not going to be
9 technically capable to serve, so it needs those assets.

10 We also want to see a reclassification of the
11 truck stop to a public water system, community water
12 system. And those were the only additions that I make.

13 Q. So those two items, the conveyance of the
14 assets and the reclassification of the public water system
15 would need to be accomplished prior to the issuance of any
16 CC&N; is that your testimony?

17 A. Certainly, yes, sir.

18 Q. And do you have anything else that you would
19 like to add to your testimony here today?

20 A. I would like to remind the Hearing Officer
21 that any utility has the opportunity to utilize the
22 Arizona Administrative Code, particularly R-14-2-406 main
23 extension agreements. Under normative circumstances a
24 utility will receive substantial assets through an advance
25 in aid of construction.

1 In this instance the developer, who is also
2 wearing the utility hat, has chosen to utilize 100 percent
3 equity, and has now placed himself in a situation that in
4 all likelihood, if he were to do it over again, maybe he
5 wouldn't do it that way. But the effect is a higher rate
6 base number that has driven rates up higher. Staff just
7 would appreciate further development utilizing the
8 financial flexibility afforded a utility through the
9 administrative code.

10 MR. SABO: Your Honor, at this time I would
11 move Exhibit S-1.

12 MR. SALLQUIST: No objection, Your Honor.
13 Thank you.

14 ALJ POPE: S-1 is admitted.

15 MR. SABO: Thank you, Your Honor.

16 Your Honor, at this time I have no further
17 questions of Mr. Fisher and he's available for
18 cross-examination.

19 ALJ POPE: Thank you.

20 MR. SALLQUIST: Thank you, Your Honor.

21

22 CROSS-EXAMINATION

23 BY MR. SALLQUIST:

24 Q. Good afternoon, Mr. Fisher.

25 A. Good afternoon, Mr. Sallquist.

1 Q. Just a couple of questions. I think we can
2 get you out of here in fine shape.

3 On the certificated area, you refer to Exhibit
4 A-10 that identified the 325 lots specifically. Would you
5 agree that that also identified the Bellemont truck stop
6 and the hotel and the associated restaurant?

7 A. Sir, I'm looking at an October 7, 2004 letter
8 from the Arizona Department of Water Resources. Is that
9 the item?

10 Q. Yes, sir, A-10.

11 A. And I'm looking at the second paragraph.

12 Q. Correct.

13 A. I would say that this letter speaks for
14 itself, in that after the 325 dwelling units, the letter
15 states the department also reviewed the nonresidential
16 demands associated with the water system, that included
17 the park and lake within Flagstaff Meadows and the
18 Bellemont truck center with its associated hotel and
19 restaurant.

20 Please note pursuant to your request the
21 department has not included Flagstaff Meadows Unit III or
22 the townhomes at Flagstaff Meadows Unit II in the demand
23 calculation. So I don't know whether or not the demand
24 was included or not included, and I believe that the
25 Department of Water Resources would be the best entity to

1 provide clarity on that.

2 Q. So it's Staff's intent, then, whatever the
3 ADWR recommends in the PAD, that would be your recommended
4 area?

5 A. It's Staff's intent to ensure that the area
6 that has demonstrated water resources is included in the
7 Phase I.

8 Q. Now, we're going to have the hydrologist on,
9 and you probably won't be able to hear. If we were to
10 demonstrate that a commercial area did not need a PAD, but
11 could be included, would that calm you as to the need for
12 a PAD for these nonresidential areas?

13 A. While I recognize that the requirements from
14 the Department of Water Resources are different for
15 commercial areas than for, say, residential subdivisions
16 associated with getting a public report, the area is
17 clearly marked undeveloped, and it could be residential or
18 it could be commercial, and the area marked Utility Source
19 may or may not be whatever.

20 All I know is that we have a very fluid
21 situation which has already resulted in a couple hundred
22 customers receiving service from an unregulated entity
23 without a certificate, and we're seeking to work with the
24 applicant to ensure that service is provided, and that the
25 applicant works with us to the extent the DWR has

1 identified 325 lots that could well have an appropriate
2 source, depending upon the rest of the letter, we say
3 again, we'll give them a certificate.

4 Q. So you're going to rely upon DWR's description
5 of what has the PAD?

6 A. Yes.

7 Q. We can certainly live with that, Mr. Fisher.

8 On the transfer of the assets, would a bill of
9 sale for those assets from the present owners to the
10 utility company as a late-filed exhibit suffice for your
11 purposes in demonstrating the ownership by Utility Source?

12 A. If it takes a contract, a bill of sale, some
13 sort of deed transference, if it had -- if you rethought
14 the financings of the utility and sought to have it
15 included in a main extension agreement, that will be fine.

16 Q. We're talking about backbone facilities
17 initially, are we not?

18 A. I believe you're talking about, since you have
19 customers that are currently receiving service and began
20 receiving service in April of '03, you're talking about
21 common plant, distribution plant, treatment plant, so
22 you're talking about everything.

23 MR. SALLQUIST: Your Honor, might I approach
24 the witness.

25 ALJ POPE: Yes.

1 Q. BY MR. SALLQUIST: Mr. Fisher, I'm going to
2 show you what's been marked as Exhibit A-3. There are two
3 schedules in there, Schedule 8 and 9, that show the
4 backbone plant, actually the water plant on one,
5 wastewater on the other. I had Mr. McCleve testify to
6 that earlier regarding the assets, and I think he said
7 there's approximately two and a half million dollars in
8 water plant shown on Schedule 8, and 1.4, 1.3 on
9 Schedule 9. Those are the backbone facilities as
10 described on that exhibit, would you agree, the upper
11 portion, the upper three quarters of Schedule 8 in
12 Exhibit A-3.

13 A. You're talking about -- I'm looking at
14 Schedule 8, Page 2 of 2, which includes service lines,
15 hydrants, backflow prevention devices, office furniture,
16 and the like. So there's a myriad of issues here.

17 Q. In the upper portion, I believe it talks about
18 backbone facilities, and the bottom four or five lines are
19 on-site facilities; is that correct?

20 A. Yes, there is a section labeled backbone
21 facilities.

22 Q. Right. And that's what I had asked
23 Mr. McCleve about when he talked about having a 2. -- was
24 it \$2.4 million investment in the water facilities?

25 A. There is a line that says total backbone

1 facilities, there is a total number of 2,409,950.

2 Q. Correct. And I think he also testified on the
3 next page about the wastewater backbone of the 1.3 in that
4 similar location?

5 A. Yes. He verified that this paper says that.

6 Q. What I'm asking you is below that are the
7 described on-site facilities, are there not?

8 A. There are some on-site facilities described
9 here, yes.

10 Q. And I think I clarified, in response to a
11 question by Mr. Sabo, that we have not yet, the company
12 has not yet entered into line extension agreements for the
13 on-site facilities; correct?

14 A. I don't recall.

15 Q. But that would be appropriate in the
16 traditional way for a utility to fund on-site facilities,
17 would it not, through line extension agreements?

18 A. Can you give me that question again, because
19 traditional way, and this application, I really have a
20 hard time.

21 Q. I understand. This is a little unique one.
22 But traditionally, site facilities are funded through the
23 406 rule that you cited previously as main extension
24 agreements; correct?

25 A. The 406 rule actually contemplates common

1 facilities as well. When you're talking about a new
2 development and raw property, raw land, a developer will
3 often include the facilities that are used for the
4 exclusive use, exclusive use of this facility. So that in
5 effect, there would be a very good argument that all of
6 the facilities would be needed for the exclusive use of
7 these, of this property, and therefore could be advanced
8 under rule 406.

9 Q. Is that the position that Staff takes on all
10 backbone facilities like that, if they're used exclusively
11 by a subdivision, they can be included in a line extension
12 agreement? Is that the normal position of Staff on
13 backbone facilities, that they can be included?

14 A. Normal position in a new CCN matter or normal
15 position where --

16 Q. In either event. Do you distinguish between
17 the two if it's a new or existing company?

18 A. Sure.

19 Q. But you do include backbone facilities in main
20 extension agreements?

21 A. Backbone facilities have been included in main
22 extension agreements that has sought and received
23 Commission approval.

24 Q. And is Staff's recommendation that the company
25 do that in this instance?

1 A. Staff has not made that recommendation in this
2 instance.

3 Q. Another recommendation you made, Mr. Fisher,
4 was regarding the reclassification of the PWS numbers.
5 You indicated that you would like to see that done before
6 the Commission would issue a certificate. Do you have
7 any idea how long that process would take?

8 A. ADEQ has issued a letter, or there's a
9 memorandum from Mr. Stuck regarding the Bellemont Travel
10 Center, and that it is currently classified as a transient
11 noncommunity.

12 Obviously, we would like to ensure that this
13 water system that is serving the public is meeting all
14 ADEQ recommendations and requirements.

15 Q. Absolutely, and we agree with that. And I
16 think Mr. McCleve testified he had informed them and he
17 would attest to the appropriate community standard, not
18 the transient.

19 But my question to you is: Do you have any
20 idea how long -- this is not a setup. I'm trying to see
21 if you know, because we do not how long it would take for
22 ADEQ to process the reclassification from a nontransient
23 to a community system.

24 A. No, I don't.

25 Q. My concern is that if it is, as often can be

1 the case in that what appears to be a simple process,
2 takes 60, 90, 120 days, would it be acceptable to Staff if
3 we had some kind of a time frame to get that
4 reclassification done as opposed to having it done prior
5 to the Commission issuing the certificate? Can we make
6 that one of the conditions? I'm asking.

7 A. We're recommending the order preliminary, and
8 that condition ought to be one of the conditions in the
9 order preliminary. So that until you accomplish that
10 situation, until you obtain that clearance from ADEQ, you
11 wouldn't have a certificate. You would be able to serve
12 as you are currently doing.

13 Q. But I guess I was under the impression your
14 recommendation was that it be an order prelim based upon
15 our providing the PAD for the area. And if we were to do
16 that prior to the judge completing the recommendation or
17 before the Commission rules later on this, they could in
18 fact issue a conditional CC&N that would say you still
19 have to provide your franchise from the county, all the
20 AOCs from ADEQ, you have to do all the things you normally
21 put in a conditional CC&N, but it would not be a
22 conditional unless we had the PAD in the file here. If we
23 don't have the PAD then my understanding was that Staff
24 would then be recommending the order prelim. Am I
25 mistaken?

1 A. Staff is recommending that in the event the
2 applicant obtain the PAD from DWR, they get a conditional
3 certificate of convenience and necessity for the defined
4 served area, which we believe is 325 lots. If you do not
5 obtain that PAD, you get an order preliminary.

6 Q. Right. Okay, and I understand that, and --

7 A. And I believe the confusion results in the
8 problematic application that has been offered here. And
9 trying to resolve it, if it's your recommendation that in
10 fact we should have, we should back away from just
11 requiring the PAD, maybe that's something we should
12 consider.

13 But we stand by our initial recommendation.
14 We're just seeking to ensure that the ADEQ
15 reclassification of the water system be accomplished as
16 part of the order preliminary for the remaining section.

17 Q. Ah, okay, so it's the reclassification for
18 what we've been referring to as Phase II here, not the
19 initial. Okay, thank you. That does, because I was
20 concerned about not being able to get the conditional CC&N
21 based upon waiting for ADEQ. Thank you, that's very
22 helpful.

23 So that I understand, then, on the bill of
24 sale you'd like to have the bill of sale on whatever we do
25 to convey the assets, you'd like to have that done before

1 even the conditional CC&N issues; is that correct? Or is
2 that before the order prelim for the Phase II area?

3 A. Let's look at the Staff report. We need to,
4 because I don't believe I have it in there.

5 Q. I didn't think you did either.

6 A. I don't believe I have it in there,
7 Mr. Sallquist. And to the extent that we are saying that
8 the Commission find a fair value at 2.3 million, the
9 Utility Source ought to have 2.3 millions of assets.

10 Q. We don't have any problem, I just want to
11 clarify the timing of filing the evidence of the assets,
12 and that's fine.

13 A. That would be good to have before we move
14 forward.

15 MR. SALLQUIST: I agree, I don't have any
16 problem with that.

17 I'm sorry to have been so long, but I thank
18 you for clarifying what we wanted. Thank you, Mr. Fisher.

19 THE WITNESS: That's quite all right.

20 ALJ POPE: Let me ask you a few questions.

21

22

EXAMINATION

23 BY ALJ POPE:

24 Q. I don't think I had Mr. Sallquist's aha moment
25 there. I'm completely confused. So if you could sort of

1 step back and summarize for me, taking into account the
2 recommendation that the asset transfer occur and that
3 there be the reclassification. Could you please put those
4 in context as the initial recommendation that Mr. Sabo
5 stated at the beginning of this hearing?

6 A. Okay. We've got a request for a certificate
7 of convenience and necessity that is primarily composed of
8 two parts, Phase I and Phase II.

9 Q. Can I stop you right there?

10 A. You bet.

11 Q. Because I thought I just understood that
12 Phase II, in your estimation, included the truck stop,
13 which needs to be reclassified.

14 A. The truck stop is a property, I believe is in
15 Phase II. I understand DWR to be talking about 325
16 dwelling units.

17 Q. So outside of 325 dwelling units which you are
18 calling Phase I, everything else is Phase II?

19 A. I believe so.

20 Q. Okay, I'm sorry, continue.

21 A. Staff and the applicant, as well as the
22 Department of Real Estate, ADEQ, and the Department of
23 Water Resources, had a number of discussions. Per those
24 discussions, it was agreed upon that in the event the
25 utility was able to obtain PAD for Phase I, Staff would

1 recommend that they obtain a conditional CC&N based on the
2 normative conditions, and that Phase II would be a
3 preliminary CC&N.

4 Now, to the extent that it is a conditional
5 CC&N for Phase I, and that one of the conditions be that
6 the Bellemont system be reclassified, I believe that would
7 be a good thing. Now, whether that makes that Bellemont
8 truck stop reclassification occur faster or slower or
9 somehow has an adverse impact on the applicant, I don't
10 know. I don't really believe there's that much of a
11 difference to make any materiality.

12 Q. So in the event they obtain the PAD, the
13 reclassification and the transfer of the offsets would be
14 a condition just as stated in your Staff report?

15 A. Yes, ma'am. Stated in my Staff report, and
16 attested to here, because I don't believe I have the asset
17 transfer.

18 Q. I meant in form and not in substance.

19 A. Thanks, I appreciate that.

20 Q. If we end up in a situation where there is no
21 PAD so we go to an order preliminary for both Phases I and
22 II, then those items are treated differently?

23 A. Yes, ma'am.

24 Q. In accordance with that order preliminary?

25 A. Yes.

1 Q. Okay. Let me just understand, if the PAD were
2 to come back from ADWR indicating that they had considered
3 more than the 325 lots in making that determination, would
4 you then include whatever they list as part of the area
5 receiving the CC&N?

6 A. Yes, ma'am. Mr. Sallquist brought up a valid
7 point in that DWR is concerned about sales to the public,
8 so they're looking at dwelling units, and the demand those
9 dwelling units have and the physical availability for
10 water resources. To the extent they're pointing out
11 undeveloped land that may or may not do whatever, from my
12 standpoint it's not appropriate to say that DWR has made a
13 determination that that would be included without DWR
14 being able to say that specifically to us on this record.

15 Q. Okay. I probably have a lot more, but I think
16 that's the majority of it.

17 A. Go ahead, don't worry about my time restraint.

18 ALJ SABO: Actually, I think that's probably
19 the vast majority of it. I can ask Mr. Johnson,
20 unfortunately for Mr. Johnson.

21 Did you have any redirect?

22 MR. SABO: No, Your Honor.

23 ALJ POPE: Thank you.

24 THE WITNESS: Thank you, ma'am.

25 (The witness was excused.)

1 ALJ POPE: I think we need to take just a
2 five-minute break.

3 (A recess ensued.)

4 ALJ POPE: We're back on the record.

5 Mr. Sallquist, were you going to call your
6 next witness?

7 MR. SALLQUIST: Yes, Your Honor. We would
8 like to call Gary Small and ask that he be sworn.

9
10 GARY G. SMALL,
11 called as a witness, having been first duly sworn by the
12 Certified Court Reporter to speak the truth and nothing
13 but the truth, was examined and testified as follows:

14

15

DIRECT EXAMINATION

16 BY MR. SALLQUIST:

17 Q. BY MR. SALLQUIST: Good afternoon, Mr. Small.

18 A. Good afternoon.

19 Q. Will you please state your name and business
20 address.

21 A. Gary G. Small. Business address is 1220 South
22 Park Lane, Suite 5, Tempe, Arizona, 85281.

23 Q. And by whom are you employed and in what
24 capacity?

25 A. HydroSystems. I am the president of

1 HydroSystems.

2 Q. How long have you been so employed?

3 A. 10 years.

4 Q. Will you please give a brief resume of your
5 personal experience in the field.

6 A. I have 30 plus years of experience in
7 hydrogeology, specializing in groundwater, groundwater
8 recharge, water supply.

9 Q. And those are the basic areas in which your
10 firm specializes?

11 A. Actually, no, those are my areas of specialty.
12 Our firm also is involved in environmental permitting,
13 groundwater modeling, aquifer treatment, and other assets
14 of groundwater recharge.

15 Q. Would you please outline the assignment your
16 firm had in connection with this project.

17 A. It had a threefold assignment. First
18 assignment was to go out and evaluate possible areas for
19 drilling a new water supply well. The second one was to
20 develop technical specifications and oversee the drilling
21 of a new water supply well. And the third one was to
22 apply and support the environmental permitting activities.

23 Q. As part of the result of your retention by
24 Utility Source, did you prepare a document that has been
25 marked as Exhibit A-8 in this proceeding?

1 A. Yes, we did.

2 Q. And that was prepared by you and your staff
3 pertaining to the subject area?

4 A. It was prepared under my supervision.

5 Q. And subsequent to the filing and preparation
6 of that, let me ask, that document was, in fact, submitted
7 to ADWR for their analysis; is that right?

8 A. Yes, it was.

9 Q. It's what's called a physical availability
10 determination analysis?

11 A. Yes.

12 Q. Subsequent to your submitting that to ADWR and
13 the company submitting a copy of that to the Commission
14 Staff, have you further reviewed and revised several of
15 the schedules in that?

16 A. Yes, we have.

17 Q. I refer you to what has been marked as Exhibit
18 A-9, and ask if those are in fact updated schedules of
19 what is contained in the original Exhibit A-8?

20 A. I don't have anything.

21 Q. I'm sorry Exhibit A-9 is the two page exhibit.
22 It appears to be Tables 1-A and 1-B.

23 A. Yes.

24 Q. Would you please give a little more
25 description of the type of analysis that you did and

1 that's contained in Exhibit A-8.

2 A. The physical availability demonstration
3 analysis is an assembly of the hydrogeologic data that's
4 available in the area, and data that we developed during
5 our work on the site itself, which includes the drilling
6 and testing of one deep well.

7 Q. Is a physical availability determination a
8 precursor to the letter of adequacy that the Department of
9 Water Resources would issue for a project?

10 A. Yes.

11 Q. Based upon your analysis, are the existing
12 water facilities sufficient to serve the entire area
13 that's been described here on Exhibit A-5?

14 A. Is the question that you're asking is there
15 water available to serve the whole area, or have we proven
16 up? What's the question?

17 Q. Why don't you answer both of them. Is there
18 water available and have you proven it up in Exhibit A-8?

19 A. First question is there is more than enough
20 water available to do the entire development. In fact,
21 the water that is being developed comes from a large
22 regional system up there that the U.S. Geological Survey,
23 City of Flagstaff and others have spent a lot of time and
24 effort to evaluate. There's more than, according to the
25 USGS, 4.8 million acre feet of water in storage and in the

1 area of the Bellemont area as well. So there's more than
2 enough water up there.

3 Q. Then the second question, have you proven that
4 up to DWR's satisfaction in Exhibit A-8?

5 A. Exhibit A-8 proves up at least enough water
6 for the 110 acre feet that they identified in their
7 letter. According to our evaluation, there's more water
8 than that available.

9 Q. Does Exhibit A-9 then also supplement that,
10 showing even additional sources or what, in addition, does
11 A-9 show?

12 A. A-9 shows some modifications to the demand
13 projections based on input that we received from DWR when
14 they initially looked at our projection demands.

15 Q. So you believe that in their further analysis
16 of what we've been calling Phase II in this proceeding,
17 they will be looking at not only the data in A-8 but also
18 that in A-9?

19 A. Yes.

20 Q. Mr. Small, I show you what has been marked as
21 Exhibit A-10.

22 Your Honor, if I may approach the witness.

23 ALJ POPE: Certainly.

24 Q. BY MR. SALLQUIST: Are you familiar with that
25 letter from ADWR to Mr. McCleve?

1 A. Yes, I saw that today for the first time.

2 Q. And that is not a physical availability
3 determination letter, is it?

4 A. No.

5 Q. How would you classify that letter from ADWR?

6 A. That is a document indicating that there will
7 be a PAD forthcoming in the amount of 110 acre feet per
8 year.

9 Q. And is that, in your opinion, adequate to
10 provide the water supply for what we've been referring to
11 here as Phase I?

12 A. Yes.

13 Q. Now, Mr. Fisher had some concern with the
14 second paragraph of that letter in that it clearly
15 indicates that the PAD is forthcoming on the 325 lots, but
16 it says they also reviewed the truck stop, hotel, and
17 related restaurant.

18 Based upon the application and information
19 that you submitted to DWR, and your understanding of the
20 process, do you believe that the PAD will in fact include
21 the truck stop, hotel, and related restaurant?

22 MR. SABO: Objection as to testimony as to
23 what DWR intends to do in the future.

24 MR. SALLQUIST: Let me rephrase it, then.

25 Q. BY MR. SALLQUIST: How do you read that letter

1 and what is your understanding of what ADWR is approving?

2 A. The second paragraph of this letter follows
3 very closely with the amended A-9 projections that we've
4 put together, which includes the parks, lakes, truck stop,
5 and hotel, as all part of that water demand.

6 Q. Do the commercial properties that are listed
7 on Exhibit A-5 as the Utility Source and also as
8 undeveloped, do those properties require the PAD from
9 ADWR?

10 A. It's unclear in my mind if they do at this
11 point.

12 Q. So you don't know if the PAD that ultimately
13 issues will in fact include those areas?

14 A. I do not know that.

15 Q. Did you submit any data to ADWR regarding
16 those demands on those properties?

17 A. We did, but that was for the full development.

18 Q. I'm sorry, I didn't understand.

19 A. We did put demand numbers in for the Phase II,
20 the full development, Phase I and Phase II.

21 Q. And would that have included what's marked up
22 there as Utility Source and as undeveloped?

23 A. Yes.

24 Q. So although the PAD that's forthcoming shortly
25 may not include it, you think perhaps the ultimate PAD

1 might include those areas?

2 A. Yes.

3 MR. SALLQUIST: Your Honor, I don't believe I
4 have any further questions of Mr. Small. I would offer
5 Exhibits A-8 and A-9 into evidence.

6 MR. SABO: No objection.

7 ALJ POPE: A-8 and 9 are admitted.

8 MR. SALLQUIST: Mr. Small is available for
9 cross-examination.

10 ALJ POPE: Mr. Sabo.

11

12 CROSS-EXAMINATION

13 BY MR. SABO:

14 Q. Good afternoon, Mr. Small. Just a couple
15 questions for you.

16 Let's start with the pond and the lake.
17 Mr. McCleve mentioned that one of the purposes of the lake
18 is for recharge; is that correct?

19 A. Presently, or in the future?

20 Q. Why don't you answer both.

21 A. In the future.

22 Q. It's intended for recharge in the future?

23 A. It will be, yes.

24 Q. And is it true that the aesthetic properties
25 of a water feature in the properties that make it

1 conducive to recharge are not the same or is that
2 incorrect?

3 A. Facilities are often multi-use facilities.
4 For example, the Town of Gilbert has one that is very much
5 multi-use.

6 Q. Is DWR, in your experience, more likely to
7 approve a recharge facility if it does not include
8 recreational aspects, or do you not know?

9 A. I don't know.

10 Q. Can you describe the difference between a
11 facility used for recharge and just a regular recreational
12 type lake?

13 A. I can. A facility that's used primarily for
14 recharge will be focused on the infiltration capacity,
15 versus a multi-use facility may focus less on infiltration
16 and more on the ability for recreation.

17 Q. And by infiltration, that's the water seeping
18 down into the ground?

19 A. Yes.

20 Q. Does that require like periodic maintenance
21 out there to make sure stuff doesn't accumulate on the
22 bottom or something?

23 A. Periodically.

24 Q. And there's also some turf, I guess, above the
25 lake, is that correct, as far as you know?

1 A. I'm not sure.

2 Q. Let me ask you this. Let's assume that there
3 is turf. If that turf were not irrigated, would that make
4 more water available for recharge?

5 A. Yes.

6 Q. And then this water feature, where it goes
7 from the recharged lake down to some sort of artificial
8 creek into a pond, does that have any recharge type
9 purpose or is that just for aesthetic purposes?

10 A. There will be some water loss, but it's mainly
11 for aesthetic purposes.

12 Q. Let me ask you some about the available water
13 supply in the area. You mentioned that there was more
14 than enough. Is there an issue about potential
15 contaminated water from the Navajo Depot, I think it's
16 called?

17 A. In my mind, no. In others' mind it's within a
18 mile radius, so they require the inspection of various
19 facilities sampling, and collecting and analysis, yes.

20 Q. By others, do you mean DWR?

21 A. DWR, DEQ.

22 Q. And can you explain the type of concerns that
23 DWR, DEQ have indicated with regard to this contamination,
24 what type is it, where is it coming from, what's the
25 history, et cetera?

1 A. Well, I can give you a little of that
2 information. That's certainly not an area that I've
3 studied. First of all, the Navajo Army Depot is located
4 to the south of this facility. The site of contamination
5 is approximately a mile south. It's surface
6 contamination, it's not at depth or down into the ground
7 water. The concern is over a hundred-year period, would
8 there be any contamination that moves from the surface all
9 the way down to the groundwater table, which is
10 approximately 15 to 1600 feet below land surface, and then
11 migrate a mile to the north and be intercepted by the
12 wells on the Bellemont property.

13 Q. And what kind of contamination are we talking
14 about here?

15 A. This is contamination from exploded ordnance.

16 Q. And what does that leave behind?

17 A. Well, it leaves behind heavy metals, for one.

18 Q. Are these the sort of things that would cause
19 drinking water quality issues, if they did migrate into
20 the water supply?

21 A. Depending on the concentrations it could,
22 obviously.

23 Q. And you're working now with part of the
24 process of getting the PAD for what people are now calling
25 Phase II, part of the process is assuaging the concerns of

1 DWR and DEQ with regard to this source of water; is that
2 correct?

3 A. Yes.

4 MR. SABO: Nothing further.

5 ALJ POPE: Can I just ask a couple questions.
6

7 EXAMINATION

8 BY ALJ POPE:

9 Q. We were talking about the issuance of the PAD
10 for specific areas, and there's been a lot of use of
11 Phase I and Phase II so I'm just going to ask you: The
12 PAD that will be issued is going to be based on current
13 use of the land; is that correct?

14 A. Yes.

15 Q. Or the immediately proposed use of the land?

16 A. Yes.

17 Q. So if there was a proposal to use some of the
18 undeveloped area for an RV park in the distant future, was
19 that conceived of in the information that you had
20 submitted?

21 A. No.

22 ALJ POPE: Okay, that's the only question I
23 had.

24 Did you have anything else, Mr. Sallquist?

25 MR. SALLQUIST: Just a couple, Your Honor.

1 REDIRECT EXAMINATION

2 BY MR. SALLQUIST:

3 Q. Mr. Small, Mr. Sabo asked you about the lake
4 use and the turf use in that area. That lake use and turf
5 use are within the area that we have been referring to as
6 Phase I, is it not?

7 A. It is, yes.

8 Q. And the analysis that you submitted to DWR and
9 what they looked at included all of those lake and turf
10 uses, did it not?

11 A. It did.

12 Q. And then on the testing, DWR requires a number
13 of quality tests as well as quantity tests, do they not?

14 A. Yes.

15 Q. And they've looked at a lot of these elements
16 that are measurable out there?

17 A. They have.

18 Q. And they will, once they issue the PAD, then
19 they stop the quality review and they shift that over to
20 ADEQ; is that correct?

21 A. That's correct.

22 Q. And the company will be subject to filing
23 tests on all of that for whatever might be appropriate in
24 the area, for the ordnance and the depot and whatever;
25 right?

1 A. Right.

2 Q. And although Mr. Sabo didn't ask this, I
3 forgot to ask you on direct; it's related to the testing.
4 Do you know what the preliminary tests show on the arsenic
5 situation for this water?

6 A. Yes.

7 Q. Would you share that with us?

8 A. All of the samples that we've collected show a
9 level below 10.

10 MR. SALLQUIST: I don't think I have any other
11 questions.

12

13

RECROSS-EXAMINATION

14 BY MR. SABO:

15 Q. To clarify that last question, by 10 you mean
16 10 parts per billion?

17 A. Yes.

18 Q. Is that the new standard that will be coming
19 into effect shortly?

20 A. Yes.

21 MR. SABO: Thank you.

22 ALJ POPE: Thank you, Mr. Small.

23 (The witness was excused.)

24 ALJ POPE: Mr. Sallquist, you had no other
25 witnesses; correct?

1 MR. SALLQUIST: We had no other witnesses.

2 ALJ POPE: Mr. Sabo, were you going to call
3 Mr. James?

4 MR. SABO: No, Your Honor, we have no further
5 witnesses.

6 ALJ POPE: I need just a second.

7 (Brief pause.)

8 ALJ POPE: Before we go to closing statements,
9 I just wanted to clarify a few things.

10 Mr. Sallquist, I asked Mr. Sabo at the
11 beginning of the proceeding whether he had a time frame in
12 mind for submittal of the PAD, and he did not indicate
13 one. I would ask that perhaps you give me a time frame in
14 which you think it's reasonable that it be filed, with the
15 understanding that during the pendency of that time, the
16 time clock for processing the application will be
17 suspended. So could you give me a time frame in which you
18 think that will be reasonable?

19 MR. SALLQUIST: Yes, Your Honor. I believe we
20 have a July 20 sufficiency date, which would put the time
21 clock at approximately December 20, so I think there are
22 two open meetings prior to that time, so hopefully we
23 won't need to suspend that.

24 We can't tell you with any great certainty
25 exactly when ADWR will issue that. We were actually

1 hopeful that we might have it today. So I think it's
2 going to be relatively soon, hopefully even before you
3 have the transcript back and start working on the order.
4 What's our worst-case? We think our worst-case might be
5 30 days on this, but we're hopeful it's more like three.

6 ALJ POPE: Okay. So just that we all
7 understand for however long it takes, if it goes beyond
8 the time frame of, I'm going to say two weeks, because
9 that's approximately the time that I'd receive the
10 transcript, then the time would be suspended until I
11 receive it.

12 And I wanted to ask both you, Mr. Sallquist,
13 and Mr. Sabo if, in your opinion, the order preliminary
14 satisfies -- the issuance of the order preliminary
15 satisfies any time clock provisions for an order being
16 issued by this Commission.

17 MR. SALLQUIST: I believe it does, Your Honor.
18 I'm not sure that the time clock rules contemplated orders
19 prelim because they weren't normally used at the time that
20 rule was issued, but I would think that they would. We
21 would not object to saying that you exceeded the time
22 clock if an order preliminary were issued.

23 ALJ POPE: Mr. Sabo, did you have an opinion?

24 MR. SABO: I would concur. I haven't gone
25 back and looked at the actual text of the time clock rule,

1 but that would make a lot of sense to me. Regardless of
2 what the text of the rule says, order preliminary
3 procedure is expressly set forth in the statute, and is
4 therefore, if the rule doesn't contemplate it, that's kind
5 of not, as long as the statute contemplates it, I think
6 we're in good shape, because obviously the statute trumps
7 the rule.

8 ALJ POPE: I wanted to ask you really quickly,
9 Mr. Sabo, not being very familiar with the procedure
10 myself, and you had mentioned earlier that it's a matter
11 of if there is an order preliminary issued, and presumably
12 there would be one in any case for Phase II, let me ask
13 you, first of all, let's assume that there is a
14 traditional CC&N for Phase I and an order preliminary for
15 Phase II. Do you conceive of those as two separate orders
16 before the Commission?

17 MR. SABO: Your Honor, it probably could go
18 either way. We don't really have a preference. I guess
19 what I was -- my conception of it was that it would be
20 bundled into one order that would grant the conditional
21 CC&N, and there will be an order preliminary for the other
22 part. But honestly, I don't think we have a strong
23 preference there or even all that weak of a preference.

24 MR. SALLQUIST: I would concur, Your Honor. I
25 think it would probably be simpler for Your Honor to

1 prepare a single order. I think that the critical thing
2 would be to make sure we have the legal description that
3 would address the two different phases.

4 ALJ POPE: I agree with that. With regard to
5 the order preliminary, setting forth the items that need
6 to be satisfied, could you then tell me, it doesn't
7 require an additional hearing, it's simply a matter of it
8 going before the Commissioners for a consideration a
9 second time?

10 MR. SABO: That's correct, Your Honor. As
11 Mr. Sallquist has indicated, the Commission has not done
12 so in a long time. I think I have run across one looking
13 back on the microfilm researching some matter or another,
14 but it's been probably since the late '70s or early '80s
15 since we've done one of those.

16 So I don't recall when they first had the ALJs
17 here, but I think it probably, that procedure predates
18 what the ALJs came into existence. So I don't know how
19 exactly the process used to work when the checklist items
20 were submitted to go from the order prelim to the CC&N.

21 It seems to me there's two possible ways that
22 could work. One would be they submit it to Staff, then
23 Staff does an open meeting item with the memorandum and
24 proposed order. And Option B would be that it's docketed
25 and then the Hearing Division prepares a proposed order.

1 Honestly, I don't think we have a preference
2 between those; whatever you would be comfortable with
3 there. Or maybe Mr. Sallquist knows how it used to be
4 done.

5 MR. SALLQUIST: Your Honor, I think you're
6 working with total cause here. It's been a long time
7 since the Commission issued one. I've got to tell you
8 they were issued in the days when the Commission would
9 issue literally one and two page orders on matters. I
10 don't think if we could find an order prelim it would give
11 you much guidance.

12 But I think Mr. Sabo's options are correct. I
13 think I would probably prefer, even though it takes a
14 little longer to have an actual order from the Commission,
15 I think the closer look at the statute does suggest it
16 requires a second order from the Commission. I think we
17 would submit whatever is required under the order prelim
18 to Staff, they would review it, that in fact it meets the
19 requirements of the initial order.

20 Based upon that, we would submit a relatively
21 brief Staff report to Your Honor, that would again prepare
22 hopefully a short order that would convert the order
23 prelim to a CC&N order that would then go to the
24 Commission. I don't believe there is a problem with doing
25 a procedural order, but again, I need to look at the

1 statute that I mis-cited to you earlier. But I think it
2 did contemplate a second order of the Commission.

3 MR. SABO: Your Honor, I agree the statute
4 requires the second order of the Commission. And perhaps
5 I wasn't clear about the two options. I was trying to
6 present where it was option one when the documentation
7 comes in, Staff prepares a memorandum and proposed order,
8 and Option B, Your Honor prepares a proposed, a
9 recommended opinion and order. But in either case, the
10 Commission would have to formally adopt the order.

11 ALJ POPE: Thank you. I think that that
12 helps.

13 Did you have a closing statement,
14 Mr. Sallquist?

15 MR. SALLQUIST: Just very briefly, Your Honor.

16 I'd like to say at the outset we are very
17 appreciative of Staff working with us, the Commission
18 Staff as well as ADWR staff. This was, as I indicated in
19 my opening statement, kind of a unique situation in that
20 we were actually providing the service prior to getting
21 some of the now obviously needed approvals. And the
22 company has indicated in Mr. McCleve's testimony, while
23 certainly not attempting to avoid any of that regulation,
24 it is just evolving development of the process, how it
25 turned out, and again with consultation with other

1 regulatory agencies, he thought he was doing what was the
2 appropriate steps. But as it turned out, it did
3 complicate life for everyone, and again, we're very
4 appreciative of Staff working with us.

5 Your Honor, we believe that a meeting that we
6 had with Staff and DWR last week was very helpful in
7 resolving this issue, to get the two stepping, if you
8 will, of this PAD, and we believe what has been discussed
9 here today is certainly a viable approach to this, and
10 provides the safeguards that the Department of Water
11 Resources needs, that the Commission needs, that the
12 customers will enjoy, and is a fair and equitable approach
13 in response to the company's application. So we believe
14 what you have heard here today is a reasonable solution.

15 Again, the company is willing to live with
16 whatever that PAD comes out in hopefully the next few
17 days. If it includes what is referred to as the Utility
18 Source parcel that's on A-5 or the undeveloped area on
19 A-5, that will be fine. And I think Mr. Fisher testified
20 he would be comfortable with that, too. If those parcels
21 are not included until we get the PAD for Phase II, that
22 certainly is acceptable to us as well. So we believe that
23 we have resolved to everyone's satisfaction how we would
24 approach this stepping approach.

25 We are very hopeful that we will have that PAD

1 shortly, so Your Honor can do as contemplated, a
2 conditional CC&N for Phase I and order prelim for
3 Phase II. We commit to you that we will get the
4 documentation to you regarding the transfer of the assets
5 to the utility company prior to your issuing a recommended
6 order in this matter. We will also work with the
7 Department of Environmental Quality on the transfer or the
8 conversion of the TWS from a transitory system to a
9 community system, and provide documentation to Your Honor
10 as quickly as we can do it on that.

11 The remaining issues, then, are something that
12 we think are quite important to the company. The first
13 has to do with the hookup fee. We believe what we have
14 proposed here is a very reasonable approach. We believe
15 that it can be distinguished from what the Staff
16 recommends in a lot of start-up companies, in that there
17 still is a lot of equity remaining in the company after
18 the full hookup fees will be collected.

19 Again, it's probably a third of the entire
20 capital of the company once the Phase II facilities,
21 different Phase II facilities are in fact built, so we
22 believe that that's a reasonable approach. Of course,
23 when you do use the hookup fee, it's a contribution, and
24 it lessens the rate base. So when we do get to that rate
25 case, whether it's a year or five years down the road,

1 that will tend to lessen the impact of those rates on
2 customers, so we believe that that is very reasonable in
3 that regard.

4 Again, the ratios of hookup fee to actual
5 capital investments we believe are consistent with things
6 that the Commission Staff has recommended in the past.

7 We also would note for the record that there
8 are a couple of instances in which the Commission has in
9 fact issued hookup fees for new companies. I certainly
10 haven't researched the record, but just quickly calling to
11 mind, I can recall at least two companies that this
12 situation has existed. One of them is a quite similar
13 situation to this. DS Water Company, which is up in
14 Mohave County, was started a number of years ago. It was
15 similar in that it was a company that was acquired by the
16 present owner of DS Water Company from a homeowners
17 association that was providing the water in an unregulated
18 fashion. That company was awarded a hookup fee. And
19 again, I don't recall the exact number, but it did receive
20 approval of some long-term financing.

21 And again, the two fit together so that you
22 can grow with the hookup fees and repay the financing.
23 Not unlike what we're proposing here, although our
24 financing, as Mr. McCleve has testified, is really kind of
25 a bridge loan situation. We don't think it makes sense to

1 pour another \$1.3 million in equity into this company when
2 it can be recovered in a reasonable fashion through a
3 hookup fee. The \$1,000 for water, the \$1800 for
4 wastewater are right in line what developers expect to
5 pay. They're shocked when they don't pay it.

6 As you know, many companies that this
7 Commission regulates, and virtually all of municipal
8 jurisdictions have hookup fees where they share some of
9 the cost of the capital for the growth with the developer.
10 We believe that is totally appropriate. And again, we
11 believe what we have proposed fits with the financing that
12 we have in place because that short-term debt can in fact
13 be refunded with the hookup fees. So we believe that it
14 may be a little different but we believe it is a good,
15 sound approach, the second company that did that.

16 And again, it's five years ago, it's perhaps a
17 different Commission, but Johnson Utility Company was a
18 start-up company that has used a hookup fee from the
19 outset. It's also for both water and wastewater. It
20 also, and don't hold me to the exact percent, but I
21 believe a 25 percent of their initial capital structure
22 was approved as long-term debt.

23 So we believe that it is not unprecedented
24 that a new utility company has both hookup fees and some
25 type of financing in place. We believe that it is in the

1 best interests of customers to do that. It's reasonable,
2 and for that reason, we would ask that you do approve
3 those.

4 The last issue that we basically had was on
5 the timing of the rate application. As Mr. McCleve
6 testified, there are going to be probably a number of
7 unknown expenses that occur in the first year of
8 operation. Even though the company has been providing the
9 services out there for several months, it probably has not
10 been accounting for those in the system that it will in
11 the future, pursuant to the NARUC accounts that Staff is
12 recommending. We're comfortable that the Commission will
13 ultimately order that, and I'm certain that the company
14 will retain appropriate, knowledgeable accounting help to
15 do that on a going-forward basis.

16 We believe that it is appropriate that this
17 Commission review this as they always do. Certainly not
18 in the first year. We don't believe that that would be
19 really needing a full analysis. And what it would
20 probably do is, with the extraordinarily high capital
21 costs for this company at the outset, because of the need
22 for those very deep wells, Your Honor can see in the
23 exhibits that there's one well there that was seven or
24 eight hundred thousand dollars. That's a lot of money for
25 a well. And they may be having to drill additional wells

1 at that depth and magnitude as part of this proving up of
2 the Phase II PAD.

3 So we believe that that company is going to
4 have a very high rate base at the end of 2005, and even
5 though it has 201 customers at this point in time, if you
6 would wait two or three or five years into the future, it
7 will have a much larger customer base over which to spread
8 those costs.

9 Again, for the benefit of the customers we
10 believe that it will be appropriate to defer having that
11 rate case and avoiding the costs because it's a start-up
12 company, it's got plenty of its own problems, it doesn't
13 need to have the burden of a rate case. They are
14 burdensome on a small company at the outset.

15 In the alternative to having a five-year full
16 blown rate case, we believe it would not be unreasonable
17 for the Commission to ask the company to file the short
18 form application which basically gives you the rate base,
19 gives you the expenses, but without all the analysis,
20 without all the supporting schedules. And if, based upon
21 that, Commission Staff analysis, they say we do need to
22 have a rate case, then the Commission will be in a
23 position they can say based upon the rate review of 2005,
24 the company should file a rate case or whatever they
25 determine appropriate at that time. To place that initial

1 burden we believe is not in the best interests of them.

2 Again, Your Honor, we appreciate very much
3 your hearing this matter and running past the closing hour
4 here to finish this today, and appreciate your
5 consideration in this matter.

6 ALJ POPE: Thank you.

7 Mr. Sabo.

8 MR. SABO: Thank you, Your Honor.

9 What the applicant is requesting and what we
10 have agreed to does represent a recommendation that is
11 unprecedented in the last several decades here at the
12 Commission, so it's certainly an important case, and one
13 that bears careful consideration, and we appreciate your
14 sticking with us through all this exciting material.

15 We would note that the way that this company
16 started up is somewhat troubling in terms of not coming to
17 the Commission from the beginning, but of providing
18 service and hooking people up without a CC&N, charging
19 rates that are not authorized. We would recommend in any
20 order that it be clear that this is not something that the
21 Commission is endorsing or approving retroactively.

22 Nevertheless, we do believe that the
23 arrangement that we have worked out is an appropriate
24 arrangement that will result, hopefully, in a conditional
25 CC&N for what we've been calling Phase I, and order

1 preliminary for Phase II. Of that, of course, assuming
2 that the Phase I PAD is submitted in a timely manner as we
3 hope that it will be.

4 Then as well, you heard Mr. Fisher testify
5 that it would be useful as one of the conditions of the
6 conditional CC&N, and one of the requirements of the order
7 preliminary, those two additional items which were the
8 transfer of offsets and the reclassification of the public
9 water system, that those items be taken care of, and so we
10 would like to see that as a -- be included in the
11 recommended order.

12 With regard to the hookup fee, I don't know
13 anything about DS Water Company so I can't comment on
14 that. I know all too much about Johnson Utilities, so let
15 me comment on that. I would hope that would not be used
16 as a model, really, for anything here. And there have
17 been numerous problems related to the way that order was
18 structured in terms of there not being a requirement to
19 come back for rate case as well as the hookup fees. And
20 in many other aspects of it we've been struggling with in
21 the aftermath of that order being granted, so I guess
22 we've got some buyer's remorse on that one. So we hope
23 that would not be used as a model, especially given the
24 problems that have been associated with that company.
25 Although to put a plug in for them, they have been helpful

1 in the AUSS matter, so I wanted to note that, since that
2 is a matter where they have helped Staff out.

3 The hookup fee is more appropriate in an
4 ongoing company where they're adding new areas to their
5 service area. Here this is a company that is starting
6 basically from a blank slate and it's basically going to
7 be one subdivision with various phases, but it's all one
8 subdivision with the same people organizing the
9 subdivision, and the same people setting the subdivision
10 up.

11 So we believe that instead of a hookup fee,
12 the appropriate thing is to have, whether through a main
13 extension or otherwise, have the developers bring that
14 equity into the company directly, rather than having a
15 hookup fee which could be passed on to consumers.
16 Especially in a case like this, where there have been
17 noncompliance issues, of course a hookup fee is something
18 where you're basically trusting the company to keep track
19 of various revenues and spend them appropriately and so
20 forth, and so we'd also have concerns about, till we get a
21 track record of compliance with this company, whether
22 allowing them those types of freedoms would be
23 appropriate.

24 With regard to the financing, we have a number
25 of concerns that it's long-term financing, that it's being

1 proposed potentially to fund ongoing operations which we
2 believe is inappropriate, that there's no principal
3 repayments required, then also that the financing is with
4 the developers, as we've seen in the hearing today,
5 there's this web of interrelated affiliated entities
6 involved in this case, and what they're asking basically
7 is to do IOUs back and forth between them.

8 I think rather than having that, and having an
9 entitlement to be repaid, we think the more appropriate
10 thing to do is to have an appropriate infusion of equity,
11 and in particular Mr. McCleve testified that this is
12 essentially for working capital purposes, and as you know,
13 working capital is included in rate base, it's considered
14 an investment, and it's appropriate that investment be
15 provided by the investor.

16 With regard to the rate application, this
17 company has been in operation for a number of years, as
18 Mr. McCleve testified. The rates were not set based on
19 any type of analysis specific to this subdivision. It's
20 appropriate that the rates be set in a rate case, that the
21 people out there have been paying rates determined by
22 Mr. McCleve for too long, and it's appropriate that they
23 get the assurance that a rate case will provide they're
24 paying the right rates.

25 We would not agree with this rate review

1 recommendation. To the extent, however, that you find it
2 persuasive, we want to be sure that if the rate review is
3 required in 2005, that there still is a requirement,
4 regardless of what is shown in the rate review, that they
5 have to come back for a rate case at a time certain,
6 within two, three, whatever years you think is
7 appropriate.

8 So those are our recommendations in this case.
9 Thank you.

10 MR. SALLQUIST: Your Honor, could I comment on
11 just a couple things?

12 ALJ POPE: If it's very brief.

13 MR. SALLQUIST: Very brief.

14 First, I don't believe Johnson Utilities has
15 had any issues regarding things that were questioned
16 today. I know there have been some issues, but that's not
17 one of them. Further, that order did require to file a
18 rate review and they did that.

19 Secondly, as to the hookup fee, Mr. Sabo
20 argues that it's designed for growth. We submit that
21 Unit III, 350 customers is growth. If you are to compute
22 the rate, the hookup fee on the million three that's going
23 to go in, and 350 customers, you probably wouldn't come
24 out with a lot different number, so we believe it is going
25 to be funded by growth, and it's not going to be paid for

1 by the present owners of the land. The hookup fee would
2 be paid for by the builder, the guy that's actually going
3 to build the house, so it is not a right pocket, left
4 pocket deal. It is funds, new money, that will be brought
5 to the party that will pay for new facilities that would
6 benefit the ratepayers.

7 Again, for the financing, we talked about it
8 as operating capital, but it really isn't so much to fund
9 the operations of the company as it is to basically get a
10 head start on the hookup fees, because the company is
11 going to have to put those large capital numbers in
12 relatively soon. It's not going to add those customers
13 that quickly, so it really isn't funding operating
14 expenses as much as it is like a bridge loan to get to the
15 capital items. Those are my comments.

16 Oh, and we wouldn't have any problem if Your
17 Honor would determine it appropriate to file a rate review
18 for 2005, and a subsequent full rate case at a later date.
19 Our objection is not to filing a rate case, it's just how
20 soon we have to file a rate case so we could certainly
21 live with a rate review, followed by a subsequent rate
22 case.

23 Thank you, Your Honor, appreciate the
24 opportunity to comment.

25 ALJ POPE: Appreciate everybody staying late.

1 And as I said before but I'd like to make clear again,
2 because I think we were all operating under the assumption
3 that the PAD is forthcoming, so the record will remain
4 open until I receive a PAD or some sort of notification
5 that it is not forthcoming, then I will issue a
6 recommended opinion and order for the Commissioners'
7 approval. Thank you all.

8 (The hearing concluded at 5:37 p.m.)

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1 STATE OF ARIZONA)
) ss.
 2 COUNTY OF MARICOPA)

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I, CECELIA BROOKMAN, Certified Court Reporter
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WITNESS my hand this 18th day of October, 2004.

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 Certificate No. 50154

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