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**BEFORE THE ARIZONA CORPORATION COMMISSION**

IN THE MATTER OF THE APPLICATION  
OF TRUXTON CANYON WATER  
COMPANY, INC. FOR APPROVAL OF A  
RATE INCREASE.

DOCKET NO. W-02168A-11-0363

IN THE MATTER OF THE APPLICATION  
OF TRUXTON CANYON WATER  
COMPANY, INC. FOR APPROVAL OF A  
REVISION OF THE COMPANY'S  
EXISTING TERMS AND CONDITIONS OF  
WATER SERVICE.

DOCKET NO. W-02168A-13-0309

IN THE MATTER OF THE APPLICATION  
OF TRUXTON CANYON WATER  
COMPANY, INC. FOR AUTHORITY TO  
INCUR LONG-TERM DEBT.

DOCKET NO. W-02168A-13-0332

Arizona Corporation Commission  
**DOCKETED**

APR 25 2014

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**VALLE VISTA PROPERTY OWNERS ASSOCIATION, INC.**

**CLOSING BRIEF**

**April 25, 2014**

1 Valle Vista Property Owners Association, Inc. (“VVPOA”) submits the following  
2 closing brief in this consolidated docket.

3 **I. BRIEF STATEMENT OF THE ISSUES AND CASE**

4 **A. VVPOA Issues of Interest Relating to Truxton’s Rate Case and**  
5 **Financing Application.**

6 VVPOA intervened in this docket to protect its interests in light of the substantial  
7 water rate increases and financings proposed by Truxton Canyon Water Company  
8 (“Truxton”) in its original rate application and separate finance application filed on  
9 September 30, 2011.<sup>1</sup> On February 15, 2013, Truxton filed “updated rate case data” with  
10 a 2012 test year.<sup>2</sup> VVPOA intervened to ensure that Truxton would charge affordable  
11 water prices to VVPOA, especially given the long prior history between VVPOA and the  
12 Neal Family Trust. Because these issues are vitally important to the community, VVPOA  
13 requests that the Commission consider and adopt the recommendations set forth below in  
14 the best interests of residential homeowners and utility customers in Valle Vista.

15 VVPOA’s recommendations relate to four issues in this consolidated docket: (1)  
16 Truxton’s rates for irrigation water supplied to VVPOA; (2) Truxton’s request for  
17 approval to finance a payment to Truxton’s owner, the Claude K. Neal Family Trust  
18 (“Trust”), for assets owned and held by the Trust that are necessary and useful for  
19 Truxton to provide water service to customers, including VVPOA; (3) Truxton’s request  
20 for financing approval to upgrade the Hualapai 1 Well from natural gas to electric  
21 service; and (4) Truxton’s request to finance, construct and operate an Arsenic Treatment  
22 Facility (“ATF”) and how those costs will be charged to customers, including VVPOA.

23 **B. Brief Summary of VVPOA’s Recommendations.**

24 On these issues, VVPOA requests that the Commission adopt the following

25 <sup>1</sup> Ex. A-1, Rate Application dated 9/30/2011; Ex. A-4, Finance Application dated  
26 9/30/2011.

<sup>2</sup> Ex. A-2, Updated Rate Case Data dated 2/15/2013.

1 recommendations based on the testimony and evidence presented in this case. VVPOA  
2 also generally supports Commission Staff's recommendations in this case. First, with  
3 respect to Truxton's irrigation rates for VVPOA, the Commission should accept Staff's  
4 proposed non-potable, irrigation rate for VVPOA of \$1.20/1,000 gallons. As  
5 demonstrated by the testimony of Ms. Brown, that rate is fair and reasonable and will  
6 cover Truxton's cost of providing service to VVPOA.<sup>3</sup> As stated in the testimony of Mr.  
7 Stewart, VVPOA can accept Truxton's proposed irrigation rates of \$1.70/1,000 gallons  
8 for the first 15,000,000 gallons of water and \$1.90/1,000 gallons for amounts above  
9 15,000,000 gallons, but only if VVPOA does not face any other increases rates or  
10 charges.<sup>4</sup> Although VVPOA can live with the \$1.70/\$1.90 rates, the evidence clearly  
11 supports the Commission Staff recommended rate of \$1.20/1,000 gallons for VVPOA.

12 Second, VVPOA requests that the Commission deny Truxton's request for  
13 approval to finance a payment to the Trust for assets owned and held by the Trust that are  
14 necessary for Truxton to provide water service to customers, including VVPOA.  
15 VVPOA agrees with Staff's finding that the Trust assets are fully depreciated with a net  
16 book value of zero. Further, Truxton proposes a flawed valuation methodology based  
17 strictly on replacement cost (without accounting for depreciation) that does not comply  
18 with the NARUC Uniform System of Accounts or the NARUC Guidelines on Cost  
19 Allocations and Affiliate Transactions. That's not to mention that under Decision No.  
20 72386, Truxton is under Commission order to acquire the Trust assets from its owner.<sup>5</sup>  
21 Truxton's attempt to turn that order into a \$1.4 million payment to the Trust financed by  
22 customers should be rejected.

23  
24 <sup>3</sup> Ex. S-3, Brown DT, Schedule CSB-22 at 2; Ex. S-4, Brown SRT, Schedule CSB-22 at  
25 2; Tr. III at 545:15-546:5 (Brown).

26 <sup>4</sup> Ex. I-4, Stewart DT at 11-12; Ex. I-5, Stewart RT at 2; Tr. II at 400:11-401:1 (Stewart).

<sup>5</sup> ACC Decision No. 72386 at 11, 19-20.

1 Third, VVPOA supports Truxton's request for financing approval to upgrade the  
2 Hualapai 1 Well from natural gas to electric service. The undisputed evidence shows that  
3 the Hualapai 1 Well is plant that is necessary for Truxton to provide adequate water  
4 service to customers, including VVPOA.<sup>6</sup> As such, VVPOA believes it is imperative that  
5 the Commission approve the financing to upgrade the Hualapai 1 Well as proposed.

6 Fourth, VVPOA supports Truxton's request to finance construction of an ATF, but  
7 the evidence demonstrates that VVPOA's rates for irrigation water should not include any  
8 charges associated with arsenic treatment. Simply put, arsenic treatment is not necessary  
9 for the non-potable irrigation water provided to VVPOA and VVPOA's irrigations rates  
10 should include an arsenic surcharge or other costs relating to arsenic treatment.

11 **II. FACTUAL BACKGROUND.**

12 The evidentiary hearing in this consolidated matter occurred on February 26-27  
13 and March 6, 2014. Truxton presented three witnesses—its manager Rick Neal and its  
14 consultants Sonn Rowell and Matt Rowell. Commission Staff presented testimony from  
15 its rate analyst Crystal Brown and engineer Dorothy Hains. VVPOA presented the  
16 testimony of its treasurer Wes Stewart.

17 **A. VVPOA is Truxton's Most Significant Water Customer.**

18 Commission Staff, Truxton and VVPOA all agree that VVPOA is a significant  
19 water customer of Truxton. At hearing, Mr. Neal testified that "the golf course is  
20 absolutely Truxton Canyon Water Company's biggest customer. They are Truxton's  
21 lifeline."<sup>7</sup> Ms. Brown acknowledged that VVPOA is a "significant revenue source" for

22 <sup>6</sup> In a letter docketed April 16, 2014 on behalf of Truxton and the Trust, B. Marc Neal  
23 stated that "Truxton Canyon Water Company and The Claude K. Neal Family Trust  
24 represent and agree that the Hualapai 1 Well is plant that is necessary for the provision of  
25 water service by Truxton. The Trust and Truxton agree that they will not sell, transfer or  
26 otherwise encumber the Hualapai 1 Well without approval of the Arizona Corporation  
Commission." April 16, 2014 letter from B. Marc Neal.

<sup>7</sup> Tr. II at 243:2-5 (Neal).

1 Truxton and that it is important to set rates for VVPOA that will allow VVPOA to  
2 continue operation and provide revenue for Truxton.<sup>8</sup> As the lifeline for Truxton,  
3 VVPOA's rates must be set in way that will allow VVPOA to continue operation, in turn  
4 serving the best interests of property owners and Truxton's residential customers.

5 The Valle Vista development is a planned community with approximately 4,300  
6 lots and 806 improved lots.<sup>9</sup> Valle Vista is located about 15 miles northeast of Kingman,  
7 just off Historic Route 66. Valle Vista is located within Truxton's CC&N area. Valle  
8 Vista has a golf course, park, tennis court and swimming pool, along with other  
9 recreational amenities.<sup>10</sup> Those facilities are center pieces of the community and are a  
10 prime selling point for the community and its residents.<sup>11</sup> Valle Vista would not be able  
11 to sustain its amenities if it weren't for the revenue derived from its assessments as well  
12 as revenue from the golf course.<sup>12</sup>

13 VVPOA is a non-profit corporation acting as the property owners association for  
14 the Valle Vista development.<sup>13</sup> The membership of VVPOA is comprised strictly of  
15 property owners in Valle Vista, including most of Truxton's residential water  
16 customers.<sup>14</sup> VVPOA's witness, Mr. Stewart, is the Treasurer and took office in  
17 November 2012. Because VVPOA is community owned and operated, any cost increases  
18 imposed on VVPOA ultimately fall on its residential property owners (*i.e.*, Truxton's  
19 residential customers) through (1) increased assessments or fees for services provided by  
20 VVPOA or (2) a drastic reduction in operation of the golf course and amenities.<sup>15</sup>

21 \_\_\_\_\_  
22 <sup>8</sup> Tr. III at 536:1-19 (Brown).

23 <sup>9</sup> Ex. I-4, Stewart DT at 1-2; Tr. II at 393: 20-25 (Stewart).

24 <sup>10</sup> Ex. I-4, Stewart DT at 2.

25 <sup>11</sup> Tr. II at 396:10-22 (Stewart); Ex. I-4, Stewart DT at 2.

26 <sup>12</sup> Tr. II at 396: 15-24 (Stewart); Ex. I-4, Stewart DT at 2.

<sup>13</sup> Ex. I-4, Stewart DT at 2.

<sup>14</sup> Ex. I-4, Stewart DT at 2.

<sup>15</sup> Tr. II at 398:5-25 (Stewart); Ex. I-4, Stewart DT at 3.

1           **B.     The Formation of Truxton in 1971 and the Trust's Water Sales to**  
2           **VVPOA.**

3           When Truxton obtained its CC&N in 1971, the Trust, as the owner of Truxton,  
4           opted to retain ownership of necessary assets for utility service, including the Hackberry  
5           Wells, the Hualapai 1 Well and the 15 mile transmission line from the Hackberry Well  
6           field to Valle Vista.<sup>16</sup> Mr. Neal's testimony on this issue speaks for itself:

7           Q.     When the CC&N was granted to Truxton in 1971 or 1972, whose  
8           decision was it to keep the transmission line, the Hackberry well field, the  
9           Hualapai well field and the storage tanks within the Trust ownership and  
10          not move those to Truxton when the Truxton CC&N was granted.

11          A.     As I understand it, the Truxton/Claude K. Neal entity, let's call it,  
12          had a law firm here in Phoenix that is the one that highly recommended that  
13          be done.

14          Q.     And do you know why they made that recommendation? Did you  
15          hear from your dad or your grandfather as to why that recommendation was  
16          made?

17          A.     *Because if – and this is just being candid – if you don't do it that*  
18          *way, the Corporation Commission will come in and take your water*  
19          *company any they want to take it.*

20          Q.     *And I have heard scuttlebutt over the years that I have been*  
21          *working on this case, that one of the reasons that your dad or your*  
22          *grandfather kept those assets within the Trust as opposed to Truxton was*  
23          *to avoid going before the ACC and having to deal with all of the*  
24          *regulatory issues. Have you heard your dad or grandfather express that*  
25          *sort of sentiment to you?*

26          A.     *Absolutely.*<sup>17</sup>

          Not only did the Trust opt to retain ownership of the water assets, but the Trust  
also decided that it – and not Truxton – would sell irrigation water to VVPOA within  
Truxton's CC&N area.<sup>18</sup> VVPOA has a long history with the Claude K. Neal Family  
Trust, which has provided irrigation water to Valle Vista since 1972. The Trust is the  
sole shareholder and owner of Truxton Canyon Water Company.

<sup>16</sup> Tr. II at 269:15-270:18 (Neal).

<sup>17</sup> Tr. II at 269:17-270:18 (Neal) (emphasis added).

<sup>18</sup> Tr. II at 315:12-19 (Neal); ACC Decision No.72386 at 12-13.

1 From approximately 1972-2011, the Trust sold irrigation water to VVPOA within  
2 Truxton's CC&N.<sup>19</sup> From 2002-2011 alone, the Trust received over \$2,000,000 in  
3 revenue from VVPOA for irrigation water.<sup>20</sup> Unfortunately, the evidence presented at  
4 hearing demonstrates that the Trust did not invest that revenue into Truxton or its  
5 regulatory assets.<sup>21</sup> On April 24, 2002, VVPOA entered an Agreement with the Trust for  
6 irrigation water. Under that Agreement, an option/renewal clause for an additional five  
7 years was made part of that Agreement. In December of 2006, the additional five year  
8 renewal clause was optioned and put into place. That Agreement between VVPOA and  
9 the Trust expired on December 31, 2011. Under that Agreement, the Trust sold water to  
10 VVPOA for \$1.14 per 1,000 gallons for water from the Hackberry Well field, with an  
11 additional \$0.35/1,000 gallons for water from the Hualapai 1 Well.<sup>22</sup>

12 At hearing, Mr. Neal testified that the agreement between the Trust and VVPOA  
13 was the "saving grace" for the Trust by ensuring guaranteed revenue to the Trust.<sup>23</sup> Mr.  
14 Neal also testified that Marc Neal and Truxton decided not to file any rate cases, instead  
15 relying on the agreement with VVPOA to provide revenue to the Trust.<sup>24</sup> As explained  
16 by Mr. Stewart, however, that water supply agreement required VVPOA to pay for 200  
17 million gallons of water each year in monthly installments even if VVPOA did not  
18 actually use the water, in effect creating an artificial revenue stream for the Trust.<sup>25</sup>

19 **C. VVPOA's Financial Situation.**

20 VVPOA's cost of water for its various community facilities is critical to its  
21 ongoing viability and that of the Valle Vista community. It is important for the

22 <sup>19</sup> Ex. I-4, Stewart DT at 6; ACC Decision No. 72386 at 12-13.

23 <sup>20</sup> Ex. I-5, Stewart RT at 6-7.

24 <sup>21</sup> Ex. I-5, Stewart RT at 6-7; Tr. II at 401: 21-25 (Stewart).

24 <sup>22</sup> ACC Decision No. 72386 at 13.

25 <sup>23</sup> Tr. II at 235:10-15 (Neal).

24 <sup>24</sup> Tr. II at 226:15-227:16 (Neal); Tr. II at 235:10-17 (Neal).

26 <sup>25</sup> Tr. II at 397:20-398:5 (Stewart); ACC Decision No. 72386 at 13, ¶29.

1 Commission to understand VVPOA's financial situation. VVPOA's fiscal year runs  
2 May1-April 31. VVPOA collects its primary revenue two times during the year—renewal  
3 of golf membership fees in December and property owner assessments in April-June. As  
4 a result, VVPOA is dependent on those sources of revenue and must budget those funds  
5 for operation of the golf course, swimming pool and other amenities during the entire  
6 year.<sup>26</sup> For the last several years, VVPOA has operated without any reserve account.<sup>27</sup>

7 VVPOA's operating expenses average approximately \$85-90,000 per month.  
8 Based on the timing of the revenue collections noted above, VVPOA experiences several  
9 months during the year where revenue is far exceeded by expenses. In 2010, VVPOA  
10 spent \$26,000 more than budget, despite cutting operating expenses by \$33,000. Even  
11 worse, revenue in 2010 was \$1,298,644, but revenue in 2011 was \$1,139,360, a decline of  
12 \$159,284.00. Even with a modest property owners dues increase, revenues remained flat  
13 in 2012 and 2013. Revenues were \$1,188,494 in 2012 and \$1,194,966 in 2013. VVPOA  
14 has been able to continue operations only by maintaining tight controls over costs and  
15 expenses. That includes water conservation for the golf course.<sup>28</sup>

16 VVPOA obtains irrigation water service from Truxton through one 3/4" meter, two  
17 2" meters, one 4" meter and one 6" meter.<sup>29</sup> As testified by Mr. Stewart, VVPOA has  
18 made operational changes in an effort to minimize water usage, but the golf course and  
19 related amenities are focal points of the Valle Vista Development.<sup>30</sup>

20 **D. Truxton's Water System.**

21 In Decision No. 41781 issued December 15, 1971, Truxton received a CC&N to  
22 provide water service in Mohave County. Truxton operates a water system that consists

23 \_\_\_\_\_  
24 <sup>26</sup> Ex. I-4, Stewart DT at 4-5.

25 <sup>27</sup> Ex. I-4, Stewart DT at 6-8.

26 <sup>28</sup> Ex. I-4, Stewart DT at 8.

<sup>29</sup> Ex. I-4, Stewart DT at 9.

<sup>30</sup> Ex. I-4, Stewart DT at 10; Tr. II at 399:15-400: 2 (Stewart).

1 of five active wells, 580,000 gallons of storage capacity and a distribution system.<sup>31</sup>  
2 Truxton served roughly 930 metered customers during the test year in this case.<sup>32</sup>

3 The Trust owns three active wells, three inactive wells, a 500,000 gallon  
4 underground storage tank, a 40,000 gallon above ground storage tank, a booster pump  
5 station, a pressure tank and a 14-16" pipeline running from the Hackberry well field to  
6 Valle Vista, approximately 15 miles long.<sup>33</sup> The three active wells are the (i) 29 Well,  
7 ADWR No. 55-564988, (ii) the Davis 2 Well, ADWR No. 55-624498 and (iii) the  
8 Hualapai 1 Well, ADWR No. 55-624999. All of those assets are necessary for Truxton to  
9 provide water service to customers.

10 Truxton is a C corporation and is wholly owned by the Trust. The Trust manages  
11 day-to-day operations of Truxton.<sup>34</sup> B. Marc Neal is the President of Truxton and the sole  
12 trustee and beneficiary of the Trust.<sup>35</sup> From 1972-2011, the Trust sold water to VVPOA  
13 within Truxton's CC&N, using the same facilities and distribution system noted above.  
14 The Trust owns and uses its wells, storage tanks and transmission main to deliver water to  
15 Truxton's distribution system. At hearing, Mr. Neal testified that the Army Corps of  
16 Engineers constructed the Hackberry transmission line in World War II to serve the  
17 Kingman air base.<sup>36</sup> Put simply, the Neal family did not install the Hackberry  
18 transmission line or incur any known costs relating to installation of the transmission  
19 line.<sup>37</sup> Mr. Neal testified that Claude Neal originally installed the Hackberry and  
20

21 <sup>31</sup> Ex. S-1, Staff Eng. Report dated 11/1/2013 at 1-5.

22 <sup>32</sup> Ex. S-1, Staff Eng. Report at 2.

23 <sup>33</sup> Ex. A-5, M. Rowell RT at 2.

24 <sup>34</sup> ACC Decision No. 72386 at 4, ¶ 3; Tr. II at 222:17-20 (Neal) ("The Claude K. Neal  
25 Family Trust that owns Truxton Canyon Water Company, and the water company, has  
26 been managed, by my father, Marc Neal, in the past for quite some years.").

<sup>35</sup> Tr. II at 222:17-26, at 334:11 (Neal).

<sup>36</sup> Tr. II at 229:17-230:16, at 272:1-5 (Neal).

<sup>37</sup> Tr. II at 272:2-12 (Neal).

1 Hualapai wells, but he could not say how much it cost to install those wells.<sup>38</sup> Further,  
2 Mr. Neal acknowledged that the Trust does not have any documentation relating to  
3 repairs to the wells, the transmission line or other assets used by the Trust/Truxton to  
4 provide water service.<sup>39</sup> Mr. Neal agreed that it is the Trust and Truxton's responsibility  
5 to provide proper documentation relating to affiliate transactions.<sup>40</sup>

6 **E. The Order to Show Cause Docket.**

7 On June 23, 2010, Commission Staff filed a Complaint and Petition for an Order  
8 to Show Cause against Truxton, alleging 16 violations of Commission statutes and  
9 regulations. On August 10, 2010, the Commission issued Decision No. 71837 as an  
10 Order to Show Cause ("OSC") against Truxton. In that docket, Truxton and Commission  
11 Staff entered a Stipulation Agreement resolving the OSC proceedings. That Agreement  
12 provided that "Truxton will acquire all water system assets necessary to provide service  
13 from the Trust no later than June 30, 2011."<sup>41</sup> In turn, the Commission issued Decision  
14 No. 72386 requiring Truxton to acquire those assets from the Trust.

15 Under Decision No. 72386, VVPOA became a customer of Truxton.<sup>42</sup> Under  
16 Decision No. 72724 issued on January 6, 2012 in Docket No. W-02168A-10-0247, the  
17 Commission entered an interim commodity rate applicable to VVPOA of \$1.45 per 1,000  
18 gallons.<sup>43</sup> In 2012, representatives of Truxton and VVPOA engaged in good faith  
19 settlement discussions on acceptable interim commodity rates and other terms that would  
20 apply to water services provided by Truxton to VVPOA. Truxton and VVPOA agreed to  
21 the following commodity rates per 1,000 gallons of water provided to VVPOA for all  
22

23 <sup>38</sup> Tr. II at 272:13-273:11 (Neal).

24 <sup>39</sup> Tr. II at 273:22-274:12 (Neal).

24 <sup>40</sup> Tr. II at 274:16-275:6 (Neal).

25 <sup>41</sup> ACC Decision No. 72386, Ex. C Stipulation Agreement at ¶4.

25 <sup>42</sup> ACC Decision No. 72386 at 18, ¶¶47-51.

26 <sup>43</sup> ACC Decision No. 72724 at 4, ¶10.

1 water provided and delivered to VVPOA through its existing 3/4", 2", 4" and 6" meters.  
2 For 0-15,000,000 gallons of water delivered each month, Truxton shall charge the rate of  
3 \$1.70 per 1,000 gallons. For over 15,000,000 gallons of water, Truxton shall charge the  
4 rate of \$1.90 per 1,000 gallons.<sup>44</sup> That is what Truxton currently charges VVPOA.

5 Here, Truxton has suggested that Commission Staff and the Commission have  
6 forced Truxton to acquire the Trust assets. In reality, Truxton voluntarily signed the  
7 Stipulation Agreement to resolve the OSC complaint with approval of B. Marc Neal:

8 Q. Mr. Neal, you had indicated in response to one of Mr. Wene's questions  
9 that Truxton was being, either the Trust or Truxton, was being ordered to  
transfer the Trust assets to Truxton. Do you recall saying that?

10 A. I do.

11 Q. Okay. And I think I can anticipate what you're probably going to answer  
12 to this and how you're going to explain it, but I'm going to ask you  
13 anyway. The Truxtons [sic] agreed, signed a stipulation agreement where  
Truxton agreed to acquire the Trust assets, agreed?

14 A. Agreed.

15 Q. And that was the order that came as a result of the order to show cause  
16 complaint filed relating to the Trust selling water within Truxton's CC&N,  
correct?

17 A. Agreed.

18 Q. Okay. Did the Trust intervene in that case and object to the transfer of  
those assets?

19 A. No.

20 Q. Did you consult your father when you signed that stipulation agreement  
21 on behalf of Truxton?

22 A. Yes.<sup>45</sup>

23 In short, when Truxton entered that Stipulation Agreement, it did so with the authority  
24 and approval of B. Marc Neal as the President of Truxton and sole trustee of the Trust.

25 <sup>44</sup> Ex. I-3, Stewart DT at 6-7.

26 <sup>45</sup> Tr. II at 288:4-25 (Neal).

1           **F. The Trust's Demand for Payment of \$1.4 Million Should Be Denied.**

2           Under Decision No. 72386, Truxton is under Commission order to acquire the  
3 Trust assets from its sole shareholder the Trust. As of today, Truxton and the Trust have  
4 not complied with Decision No. 72386. Mr. Neal justified that non-compliance by  
5 stating that "the Trust will not give those assets away, period."<sup>46</sup> He also testified that it  
6 is in Truxton's best interests for Truxton to own the Trust assets necessary to provide  
7 water service.<sup>47</sup> Mr. Neal explained that the Trust does not oppose transferring assets to  
8 Truxton, but the issue is financial compensation to the Trust.<sup>48</sup> In turn, Truxton proposes  
9 that the Commission approve the Company's arbitrary \$1.4 million purchase price for the  
10 Trust assets or, alternatively, that the Commission authorize the Trust to sell water to  
11 Truxton at \$1.70 per 1,000 gallons.<sup>49</sup>

12           In response to questions from his attorney, Mr. Neal explained how *he and Mr.*  
13 *Wene* came up with the \$1.4 million purchase price for the Trust assets:

14           Q. Explain how that was arrived at. Did you have a higher number at the  
15 beginning?

16           A. I had a much higher number at the beginning.

17           Q. And how was that number determined?

18           A. I said, and correct me if I'm wrong, but I said, I think my first question  
19 was how are the customers going to pay for it. Secondly I said, well, we  
20 need to discount this significantly if it's going to happen, and it's just the  
assets, and the Trust owns the company anyway. So if we're just selling the  
assets, let's discount it a ton and, and do it for like \$3 million. And you [Mr.  
Wene] laughed at me.

21           Q. Okay. And let's just back up. The initial estimate that you had for the  
22 value of this was around 10 million?

23           A. Correct.

24 <sup>46</sup> Tr. II at 256:817-18 (Neal).

25 <sup>47</sup> Tr. II at 328:24-329:11 (Neal).

26 <sup>48</sup> Tr. II at 330:5-11 (Neal).

<sup>49</sup> Tr. II at 263:20-264:6 (Neal); Tr. II at 278:10-12 (Neal).

1 Q. Okay. And then you said, severely discount it. And you came up with a  
2 number of –

3 A. \$3 million.

4 Q. And then continue.

5 A. And you told me, no way. And I said, what do you, what do you mean,  
6 no way? It's worth far more than that. And you said well, the ACC is never  
7 going to buy it. *And we ended up, you and I together, coming up with an  
8 arbitrary number of \$1.4 million, because once below three it was like  
9 ridiculous. And I said, okay, well, if it works at 1.4, I'll tell the Trust that  
10 that's what has to be done.* And that's how the number -- it was -- And you  
11 know, we sat here all day yesterday arguing about this -- I mean, there was  
12 hours of testimony over this 1.4 -- that's how simple it was. There was no  
13 science to it. That's how we came up with the \$1.4 million. Is it, is it far less  
14 than the assets are worth? I don't care how you slice it, it is. It's far less  
15 than the assets are worth. But should it be done? I don't think it should, but  
16 that's just my opinion.<sup>50</sup>

17 Mr. Neal went on to testify that his original \$10 million estimate for the Trust assets came  
18 from “the sky” and was a “rough guess on [his] part.”<sup>51</sup> Mr. Neal also testified that there  
19 was an offer to buy Truxton as a whole for \$2,500 per connection (or roughly \$2.25 M)  
20 several years ago.<sup>52</sup> Apparently the entire company is worth \$2.25 million, but the Trust  
21 assets are worth \$10 million—at least according to Mr. Neal and Mr. Wene.<sup>53</sup>

22 Mr. Neal also conceded that the wells and transmission line are old and in need of  
23 repairs and upgrades; and that the only use of the transmission line is for service to

24 \_\_\_\_\_  
25 <sup>50</sup> Tr. II at 260:15-262:5 (R. Neal) (emphasis added). In offering this testimony at hearing  
26 relating to how Mr. Neal and Mr. Wene determined the \$1.4 million purchase price for  
the Trust assets, Mr. Neal and Truxton have waived any attorney-client privilege on this  
issue. With respect to the \$1.4 million transfer price, Mr. Rowell also testified that “I  
believe Mr. Neal and Mr. Wene determined it. You know, they thought it was a number  
that was fair and that could, you know, resolve the issues in this case in a manner that was  
fair to everyone.” Tr. I at 130:6-9 (M. Rowell).

<sup>51</sup> Tr. II at 289:6-8 (Neal)

<sup>52</sup> Tr. II at 289:12-25 (Neal).

<sup>53</sup> Tr. II at 290:1-14 (Neal)(“Q. And then ultimately, you and Mr. Wene discussed the  
numbers, and you guys ultimately decided to ask for \$1.4 million, agreed? A. Yes. Q.  
Okay. And I think what you said was there was no science to it, that was just a number  
that you came up with, fair? A. Fair.”).

1 Truxton's customers.<sup>54</sup> And he admitted that neither Truxton nor the Trust had any  
2 depreciation analysis done relating to the Trust assets.<sup>55</sup> Mr. Neal likewise conceded the  
3 proposed sale of assets between the Trust and Truxton is not an arm's length  
4 transaction.<sup>56</sup> In fact, Mr. Neal acknowledged that "if the Trust were to transfer the plant  
5 assets from its, from its own name into the name of the water company, it would still own  
6 the same plant that it currently owns."<sup>57</sup>

7 Mr. Neal alternatively proposed that the Commission authorize the Trust to retain  
8 the assets and sell water to Truxton for \$1.70 per 1,000 gallons. On this issue, Mr. Neal's  
9 testimony is equally self-serving with respect to the Trust's interests:

10 Q. What is the Trust's actual cost per 1,000 gallons of water supplied to  
11 Truxton?

12 A. I don't know how to answer that question. And the reason being is  
13 because it all depends on which well field it's coming from, which time of  
14 year it's being served, and what is included in those costs. Because if, if  
15 you're just talking the actual pumping cost, then that's different than if  
16 you're talking the cost of delivering the water to the customer....

17 Q. Have you undertaken any analysis of what it costs the Trust to supply the  
18 water on that type of basis?

19 A. No.

20 Q. Okay. Has the Trust provided you with any information as to what it  
21 actually costs them to send the water down the pipeline?

22 A. No.

23 Q. Okay. You would agree that when you're setting a price for water being  
24 sold from the Trust to Truxton, it's probably a relevant inquiry to figure out  
25 exactly what it costs the Trust to produce the water, agreed?

26 A. Not necessarily.

Q. Why not?

---

24 <sup>54</sup> Tr. II at 291:11-292:6 (Neal).

25 <sup>55</sup> Tr. II at 295:3-13 (Neal).

26 <sup>56</sup> Tr. II at 296:10-15 (Neal).

<sup>57</sup> Tr. II at 312:14-18 (Neal).

1 *A. Because, for the same reason that when we are told that the assets are*  
2 *completely depreciated and the water company is worth zero, and the*  
3 *Trust says no it's not, this is the price. If, if the Trust is willing to sell*  
4 *water for \$1.70 and they're not incurring the expenses, that's their call.*  
5 *They can put a number on that, whatever number they want. You can sell*  
6 *your car for whatever price you want to sell your car for.*

7 Q. But you understand here that the Truxton customers are within a  
8 monopoly service area for Truxton. Do you understand what I mean by  
9 that?

10 A. Yeah.

11 Q. In other words, they can't get water from anybody else because they're  
12 within Truxton's CC&N, correct?

13 A. Correct.

14 Q. And you also said before that the Trust is the sole shareholder and owner  
15 of Truxton, agreed?

16 A. Right....

17 Q. You would agree, Mr. Neal, that if it actually cost the Trust 75 cents per  
18 1,000 gallons to send water from the Hackberry field down the transmission  
19 line to Valle Vista, that a request for \$1.70 would be high, would it not?

20 A. I would say no. And the reason that I would say no is because of the  
21 years' worth of cost that has been spent by the Trust that have never been  
22 compensated, I would say not at all.<sup>58</sup>

23 To say Mr. Neal's justifications for the proposed prices imposed by the Trust on Truxton  
24 and its customers are not persuasive and unsupported is an understatement.

25 Fundamentally, Mr. Neal's testimony on these various issues illustrates the  
26 fundamental conflict of interest underlying the internal dealings between the Trust and  
Truxton. As noted in Decision No. 72386, Commission Staff concluded "that there is no  
independent management protecting Truxton's rights against the Trust, and that the Trust  
should not be selling water within Truxton's CC&N. Staff testified that the Agreement  
with the Association, as well as other agreements, have been signed by B. Marc Neal on  
behalf of the Trust and that a conflict of interest exists because Mr. B. Marc Neal acts as

<sup>58</sup> Tr. II at 278:10-281:23 (Neal) (emphasis added).

1 both President of Truxton and as the sole Trustee of the Trust.”<sup>59</sup> Those same findings  
2 apply here relating to the proposed sale of Trust assets to Truxton.

3 **III. VVPOA’S NON-POTABLE IRRIGATION WATER RATES.**

4 **A. The Commission Should Adopt Commission Staff’s Recommended**  
5 **Irrigation Rate for VVPOA.**

6 At hearing, Commission Staff (Crystal Brown) proposed an irrigation water rate  
7 for VVPOA of \$1.20 per 1,000 gallons.<sup>60</sup> Obviously, VVPOA would prefer that the  
8 Commission adopt Commission Staff’s proposed rates for irrigation water. Ms. Brown’s  
9 proposed rates are based on Truxton’s operating expenses and costs of providing service  
10 to VVPOA.<sup>61</sup> Truxton’s rates for VVPOA should be based on cost of service.<sup>62</sup>

11 In this rate case, Truxton did not provide any cost of service testimony or other  
12 justification supporting increased tariff rates for VVPOA. In fact, Truxton’s witnesses do  
13 not even know what it costs Truxton or the Trust to provide water to customers or  
14 VVPOA on a per 1,000 gallon basis.<sup>63</sup> The evidence presented at hearing demonstrates  
15 that Truxton (and the Trust) incur minimal costs in providing water service to VVPOA.

16 Under the prior agreements with VVPOA, the Trust provided water to VVPOA for many,  
17 many years at substantially lower rates. The Truxton water system is a gravity feed  
18 system from the Hackberry well field and the evidence demonstrates that Truxton and the  
19 Trust do not incur significant costs of providing water to customers.<sup>64</sup> Obviously,  
20 Truxton has the burden of supporting its proposed irrigation rates and Truxton must face

21 <sup>59</sup> Decision No. 72386 at 13-14, ¶ 31.

22 <sup>60</sup> Ex. S-5, Brown RT, Schedule CSB-22 at 2; Tr. III at 545:15-19 (Brown).

23 <sup>61</sup> Tr. III at 545:20-24 (Brown).

24 <sup>62</sup> *See Principles of Water Rates, Fees and Charges, Manual of Water Supply Practices,*  
25 *American Water Works Association (5<sup>th</sup> Ed. 2000) at p. 49 (“The basic premise in*  
*establishing adequate rate schedules that are equitable to different customers is that rates*  
*should reflect the cost of providing water service.”)*

26 <sup>63</sup> Tr. I at 154:20-155:7 (M. Rowell); Tr. II at 278:13-279:7 (Neal).

<sup>64</sup> Tr. II at 245:2-12 (Neal); Ex. S-14, 2/5/2012 letter from R. Neal to V. Burns at 2.

1 the consequences of failing to present any supporting testimony or evidence.

2 Unlike Ms. Rowell or Mr. Neal, Ms. Brown's recommendation was based upon  
3 her "regulatory audit of the company's rate case application, operating expenses, invoices,  
4 [and] costs..."<sup>65</sup> Ms. Brown testified that the \$1.20/1,000 gallons rate is fair and  
5 reasonable for VVPOA.<sup>66</sup> Further, Ms. Brown emphasized that Truxton has never  
6 provided any numbers on the actual cost of sending water from the Hackberry well field  
7 to VVPOA or any of Truxton's customers.<sup>67</sup> In fact, Exhibit S-14 – a February 5, 2012  
8 letter from Rick Neal to ADEQ – documents that Truxton incurs minimal costs in  
9 providing water to customers from the Hackberry well field. As stated by Mr. Neal, "[i]t  
10 is relatively inexpensive to lift the water from the shallow wells and gravity flow it  
11 downhill to the customers."<sup>68</sup> That sentence is consistent with Staff's recommended rates  
12 for irrigation water provided to VVPOA.<sup>69</sup> Staff concluded that its recommendations are  
13 appropriate and Truxton "is making enough to pay its bills and probably more" based on  
14 the information provided by Truxton.<sup>70</sup> Truxton simply did not provide "any operational  
15 data on what it takes to provide water to [VVPOA], nor to the Trust."<sup>71</sup> Put simply,  
16 Truxton did not provide information "that would show the cost to run Truxton."<sup>72</sup>

17 Further, on September 1, 2010, the Trust and Truxton entered a "Water Supply  
18 Agreement for Truxton Canyon Water Company." Paragraph 8 of that Agreement  
19 establishes Truxton's cost of purchasing water at \$1.01 per 1,000 gallons delivered,  
20 including a return on the value of the Trust assets necessary to provide service:

21 \_\_\_\_\_  
22 <sup>65</sup> Tr. III at 545:20-24 (Brown).

23 <sup>66</sup> *Id.* Tr. III at 545:25-546:3 (Brown).

24 <sup>67</sup> Tr. III at 545:4-9 (Brown).

25 <sup>68</sup> Ex. S-14, 2/5/2012 letter from R. Neal to V. Burns at 2.

26 <sup>69</sup> Tr. III at 547:8-11 (Brown).

<sup>70</sup> Tr. III at 569:6-8 (Brown).

<sup>71</sup> *Id.* at 569:1-5 (Brown).

<sup>72</sup> Tr. III at 569:23-570:5 (Brown).

1 Truxton Canyon shall pay to Trust all metered water deliveries at the agreed  
2 upon delivery points at the rate of \$1.01 per 1000 gallons delivered. That  
3 price shall be subject to review on each anniversary date of the Agreement,  
4 but will not be changed except upon 90 days written notice to Truxton  
5 Canyon. *Said price will be based upon the market value of the water  
6 considering the operation, maintenance and capital cost to Trust, plus a  
7 return on the value of the equipment and facilities necessary to provide  
8 service under this Agreement.*<sup>73</sup>

9 That agreed pricing between the Trust and Truxton supports Ms. Brown's  
10 recommendations here. Mr. Neal did not perform any cost analysis to dispute Ms.  
11 Brown's recommended rates. In terms of the irrigation rate for VVPOA, Ms. Rowell did  
12 not even bother reviewing the recommendations of Ms. Brown.<sup>74</sup>

13 **B. Truxton's Proposed Rates for VVPOA.**

14 As noted in Mr. Stewart's testimony, if the Commission deviates from  
15 Commission Staff's recommended rates, VVPOA can accept a rate of \$1.70/1000 gallons  
16 for the first 15,000,000 gallons per month provided to VVPOA (across all of its meters)  
17 and \$1.90 per 1,000 gallons for any amounts above 15,000,000 gallons (again, across all  
18 of its meters).<sup>75</sup> Those are the rates proposed by Truxton in its updated rate case filing.  
19 VVPOA believes it can afford to pay those rates—provided that VVPOA's rates do not  
20 increase resulting from the ATF or Truxton's proposal to finance \$1.4 in assets to be  
21 purchased from the Trust. As testified by Mr. Stewart, the proposed rates of \$1.70/\$1.90  
22 "is basically all that [VVPOA] can afford."<sup>76</sup>

23 **IV. TRUXTON'S REQUEST TO FINANCE A \$1.4 MILLION PAYMENT TO  
24 ITS OWNER SHOULD BE DENIED.**

25 VVPOA requests that the Commission deny Truxton's request for approval to  
26 finance a payment to the Trust for assets that are necessary for Truxton to provide water

<sup>73</sup> Ex. S-6, Water Supply Agreement for Truxton Canyon Water Company dated 9/1/2010  
at 3, ¶ 8; *see also* Ex. I-1, 1991 Water Supply Agreement at 3, ¶8.

<sup>74</sup> Tr. I at 40:8-41:9 (S. Rowell).

<sup>75</sup> Tr. II at 400: 19-401: 1 (Stewart).

<sup>76</sup> Tr. II at 391:5 (Stewart).

1 service to customers, including VVPOA. VVPOA simply can't afford to pay a surcharge  
2 or finance charge for the \$1.4 million payment to the Trust.<sup>77</sup>

3 **A. The Trust Assets Have a Net Book Value of Zero and Truxton's**  
4 **Valuation Methodology Does Not Comply With NARUC Standards.**

5 VVPOA agrees with Staff's finding and conclusions that the Trust assets are fully  
6 depreciated with a net book value of zero.<sup>78</sup> Ms. Brown's testimony is undisputed that all  
7 of the Trust assets have reached the end of their depreciable life and have a net book  
8 value of zero for purposes of the proposed transfer to Truxton. The substantial evidence  
9 in this case demonstrates that Trust should not receive any financial compensation for  
10 transfer of the Trust assets to Truxton. That's true on several levels.

11 To start, as established at hearing, Truxton proposes a flawed valuation  
12 methodology based strictly on replacement cost (without accounting for depreciation) that  
13 does not comply with the NARUC Uniform System of Accounts or the NARUC  
14 Guidelines on Cost Allocations and Affiliate Transactions.<sup>79</sup> Section 104(A) of the  
15 NARUC Uniform System of Accounts for Class C Utilities provides: "[t]his account shall  
16 be temporarily charged with the cost and expense incidental to acquisition of utility  
17 systems acquired as operating units or systems."<sup>80</sup> Section 104(B) provides that "[i]n  
18 clearing this account the original cost of acquired plant shall be charged to plant accounts,  
19 and accumulated depreciation shall be credited to account 108 – Accumulated  
20 Depreciation and Amortization of Utility Plant in Service."<sup>81</sup> Section 114 goes on to state  
21 that "any balance representing the difference between the net original cost of the assets  
22

23 <sup>77</sup> Tr. II at 391:24-392:1 (Stewart).

24 <sup>78</sup> Tr. II at 401:9-12 (Stewart); Ex. I-5, Stewart RT at 5-6.

25 <sup>79</sup> Ex. I-3, NARUC Uniform System of Accounts for Class C Utilities at 24-26.

26 <sup>80</sup> Ex. I-3, NARUC Uniform System of Accounts at 24, § 104(A).

<sup>81</sup> Ex. I-3, NARUC Uniform System of Accounts at 24, § 104(B); Tr. at 166:24-167:7 (M. Rowell).

1 acquired and the cost to the acquiring utility shall be charged or credited to Account 114 –  
2 Utility Plant Acquisition Adjustments.”<sup>82</sup>

3 Further, § 104(C) provides: “[w]hen an existing water system or operating unit is  
4 acquired, the utility shall be obligated to obtain from the vendor all existing records,  
5 including records of plant construction dates and costs, records of accumulated  
6 depreciation applicable to such properties, and records of contributions in aid of  
7 construction.”<sup>83</sup> Again, neither Truxton nor Mr. Rowell requested that the Trust provide  
8 documentation regarding accumulated depreciation of the Trust assets.<sup>84</sup> Finally, § 108 of  
9 the NARUC standards provides that “this account shall be credited with accounts  
10 representing the balance of accumulated depreciation and amortization of utility plant  
11 acquired from others.”<sup>85</sup>

12 At hearing, Mr. Rowell conceded that these NARUC standards apply to Truxton  
13 and that the NARUC standards apply to accounting for rate cases. Even so, Mr. Rowell  
14 did not apply or consider the NARUC standards in his valuation opinions.<sup>86</sup> Ms. Brown  
15 also testified that Truxton is obligated to comply with the NARUC Uniform System of  
16 Accounts for Class C Utilities, including the requirements for accounting of depreciation  
17 with respect to assets acquired from another entity.<sup>87</sup> Ms. Brown expressly testified that  
18  
19

20 \_\_\_\_\_  
21 <sup>82</sup> Ex. I-3, NARUC Uniform System of Accounts at 24, § 114; Tr. I at 167:8-14 (M.  
22 Rowell).

23 <sup>83</sup> Ex. I-3, NARUC Uniform System of Accounts at 25, § 104(C); Tr. I at 167:20-168:4  
24 (M. Rowell).

25 <sup>84</sup> Tr. I at 122:3-6 (M. Rowell); Tr. I at 50:15-18 (S. Rowell); Tr. I at 120:1-3 (M.  
26 Rowell); Tr. I at 128:1-129:4 (M. Rowell); Tr. II at 295:3-13 (Neal).

<sup>85</sup> Ex. I-3, NARUC Uniform System of Accounts at 25, § 108.; Tr. I at 169:24-170:5 (M.  
Rowell).

<sup>86</sup> Tr. I at 165:4-20 (M. Rowell).

<sup>87</sup> Tr. III at 547:22-548:10 (Brown).

1 those NARUC Standards are consistent with her recommendations regarding valuation of  
2 the Trust assets and the terms and conditions of the NARUC Guidelines.<sup>88</sup>

3 In addition to the NARUC standards, Ms. Brown applied the NARUC Guidelines  
4 for Cost Allocations and Affiliate Transactions to the proposed sale between Truxton and  
5 the Trust. Almost inconceivably, Mr. Rowell did not consider or apply the NARUC  
6 Guidelines (Ex. S-8), even though he used and applied those guidelines as a witness for  
7 RUCO and Global Water in other rates cases.<sup>89</sup> Those Guidelines speak for themselves:

8 Generally, transfer of a capital asset from the utility to its non-regulated  
9 affiliate should be at the greater of prevailing market price or net book  
10 value, except as otherwise required by law or regulation. **Generally,**  
11 ***transfer of assets from an affiliate to the utility should be at the lower of***  
***prevailing market price or net book value, except as otherwise required by***  
***law or regulation.*** To determine prevailing market value, an appraisal  
should be required at certain value thresholds as determined by regulators.<sup>90</sup>

12 Under those Guidelines, “prevailing market pricing” is defined as “a generally accepted  
13 market value that can be substantiated by clearly comparable transactions, auction or  
14 appraisal.”<sup>91</sup> Truxton did not present any comparable transactions or auction results.

15 Further, the NARUC Guidelines dictate that the cost for the Trust assets shall be at  
16 the **lower** of prevailing market price or net book value. As conceded by both Ms. Rowell  
17 and Mr. Rowell, net book value requires reducing original book value by accumulated  
18 depreciation.<sup>92</sup> Here, Truxton did not present any evidence relating to accumulated  
19 depreciation, which means that Ms. Brown’s testimony is undisputed that the Trust assets  
20 are fully depreciated, in turn rendering the net book value at zero.

21  
22  
23 <sup>88</sup> Tr. III at 548:4-10 (Brown), at 549:8-551:1 (Brown).

24 <sup>89</sup> Tr. I at 171:10-172:11 (M. Rowell).

25 <sup>90</sup> Ex. S-8, NARUC Guidelines for Cost Allocations and Affiliate Transactions, at 4,  
§ D(3).

26 <sup>91</sup> Ex. S-8, NARUC Guidelines at 2, § 12.

<sup>92</sup> Tr. I at 58:6-16 (S. Rowell); Tr. I at 176:19-21 (M. Rowell).

1           **B. Truxton's Attempt to Finance Affiliate Profit Should be Rejected.**

2           Boiled down, the \$1.4 million proposed price for the Trust assets is nothing more  
3 than affiliate profit to the Trust that should be rejected under the evidence presented at  
4 hearing. Specifically, the Neal Family formed Truxton in 1972 as a regulated utility, but  
5 decided to retain title of the assets necessary to provide service in the Trust in order to  
6 avoid Commission regulation and allow the Trust to sell water to VVPOA within  
7 Truxton's CC&N. In turn, the Trust received substantial revenue from selling water to  
8 Truxton and selling irrigation water to VVPOA, including a return on the Trust assets.  
9 Truxton now proposes that customers finance a \$1.4 million payment to the Trust for  
10 those very same assets used by the Trust to generate revenue for 40 years. Even after  
11 such sale, the Trust will still own those assets as the sole shareholder of Truxton.

12           Ms. Brown explained Staff's opposition to this type of transaction: "And in the  
13 case of a transfer of an asset, the service provided by that asset is the same for the  
14 customers after the asset has been transferred. There has been no improvement in the  
15 service to the customers, so the customers should not have to pay an additional cost to  
16 receive the same service. So there should be no level of profit included."<sup>93</sup>

17           Under the NARUC Guidelines, Ms. Brown explained Staff's depreciation analysis  
18 relating to the Trust assets, ultimately concluding those assets have been fully  
19 depreciated.<sup>94</sup> Commission Staff submitted a data request to Truxton requesting  
20 documentation relating to the \$1.4 million purchase price for the Trust assets, but Truxton  
21 did not provide any documentation relating to that price or depreciation.<sup>95</sup> She also  
22 testified that neither Truxton nor Mr. Rowell provided any documentation of repairs  
23 made to the Trust assets that extended the depreciable life of those assets.<sup>96</sup> As a result,

24 <sup>93</sup> Tr. III at 539:21-540:2 (Brown).

25 <sup>94</sup> Tr. III at 541:1-5 (Brown).

26 <sup>95</sup> Tr. III at 541:4-21 (Brown).

<sup>96</sup> Tr. III at 542:2-19 (Brown).

1 the only evidence presented in this case assets was that those assets have been fully  
2 depreciated using accepted depreciation rates for those assets.<sup>97</sup>

3 On these issues, Ms. Brown went on to testify as follows:

4 Q. If we assume that the assets are fully depreciated -- Ms. Brown, you're  
5 also aware that the Trust used those assets to sell water to Valle Vista  
6 Property Owners Association, correct?

6 A. Yes.

7 Q. And did you review Mr. Stewart's testimony in this case?

8 A. I looked at some of it, yes.

9 Q. Were you aware that he testified that roughly between 2010, or 2002  
10 and 2010, VVPOA paid the Trust over \$2 million for water provided from  
11 the Hackberry well field down the transmission line?

11 A. Yes. I heard that testimony.

12 Q. And were you present for Mr. Neal's testimony when I asked him  
13 whether the Trust owns those assets free and clear and whether they are  
14 subject to any debt financing or mortgage obligations, or anything like that?

14 A. I heard that testimony.

15 Q. And is it your understanding that the Trust owns those assets free and  
16 clear?

16 A. Yes.

17 Q. And if those assets are fully depreciated, and the Trust had earned \$2  
18 million from the Association, would you agree that the \$1.4 million that  
19 they're asking for here would essentially be the equivalent of owner profit  
20 here?

20 A. Yes.

21 Q. And that would be reflected in the fact that the owner doesn't have any  
22 debt obligations, the original assets may have actually been installed by  
23 other parties, the owner had used those assets to obtain substantial revenues  
24 over the years, and the current condition of the those assets as reflected in  
25 the depreciation analysis, fair?

24 A. Yes.<sup>98</sup>

25 <sup>97</sup> Tr. III at 542:13-25 (Brown).

26 <sup>98</sup> Tr. III at 543:1-545:14 (Brown).

1 Ms. Brown also testified that it is unlikely that WIFA would even approve financing for a  
2 utility to pay its sole owner and shareholder for aged and deteriorated assets.<sup>99</sup>

3 Ultimately, Ms. Brown testified that “at no time have I seen the Commission  
4 approve a company selling to itself.”<sup>100</sup> Ms. Brown also testified that the “market based  
5 price of the Trust assets” is “zero, net book value is zero.”<sup>101</sup> As stated by Ms. Brown,  
6 “Mr. Rowell did not use any cost documentation in developing his estimate.”<sup>102</sup> Aside  
7 from the express requirements of NARUC, the Trust should not receive a \$1.4 million  
8 payment financed by customers for selling assets to itself under these circumstances.

9 **C. Truxton’s Proposed Valuation for the Trust Assets is Flawed.**

10 On these issues, the testimonies of Sonn Rowell and Matt Rowell are entirely  
11 unpersuasive and, in fact, support Staff and VVPOA. To start, Ms. Rowell testified that  
12 Truxton is obligated to comply with the NARUC Uniform System of Accounts for Class  
13 C. utilities.<sup>103</sup> With respect to the NARUC Guidelines, Ms. Rowell agreed that “net book  
14 value” means “taking the original cost or book value and netting that number out for  
15 depreciation...”<sup>104</sup> Yet Ms. Rowell did not perform any depreciation analysis relating to  
16 the Trust assets, she did not know when those assets were installed or put into service and  
17 she does not know what depreciation rates apply to those assets.<sup>105</sup> She also has never  
18 seen a situation where the sole shareholder of a regulated utility owns wells or pipelines  
19 and then sells them to the regulated utility which the shareholder also owns.<sup>106</sup>

20 Mr. Rowell’s testimony is equally unpersuasive relating to valuation of the Trust

21 \_\_\_\_\_  
22 <sup>99</sup> Tr. III at 543:1-545:14 (Brown).

23 <sup>100</sup> Tr. III at 588:17-18 (Brown).

24 <sup>101</sup> Tr. III at 589:2-4 (Brown).

25 <sup>102</sup> Tr. III at 593:20-21 (Brown).

26 <sup>103</sup> Tr. I at 50:1-14 (S. Rowell).

<sup>104</sup> Tr. I at 58:8-15 (S. Rowell).

<sup>105</sup> Tr. I at 78:10-16 (S. Rowell).

<sup>106</sup> Tr. I at 68:2-7 (S. Rowell).

1 assets. To start, Mr. Rowell admitted that he did not follow the NARUC Uniform System  
2 of Accounts or the NARUC Guidelines in his testimony. Rather, Mr. Rowell applied a  
3 “reconstruction cost study” to determine a hypothetical valuation of the Trust assets. Mr.  
4 Rowell is not a certified appraiser<sup>107</sup> and he did not justify his use of a reconstruction  
5 valuation without accounting for depreciation of the assets.

6 In his testimony, Mr. Rowell acknowledged that the NARUC Uniform System of  
7 Accounts requires evaluation of depreciation relating to the Trust assets; yet Mr. Rowell  
8 did not perform any depreciation analysis.<sup>108</sup> The purpose of Mr. Rowell’s replacement  
9 cost new study was to determine “what is it going to cost to replace this today.”<sup>109</sup> He also  
10 noted that the “nature of the assets in the ground aren’t really important for that.”<sup>110</sup> Mr.  
11 Rowell’s testimony is more memorable for what he didn’t do than what he did do:

- 12 • Mr. Rowell did not know and did not consider the age and/or  
13 condition of the Trust assets in determining valuation of the Trust  
assets.<sup>111</sup>
- 14 • Mr. Rowell did not perform any depreciation analysis and he does  
15 not know the depreciable life of any of the Trust assets.<sup>112</sup>
- 16 • Mr. Rowell claims that the Trust assets are not fully depreciated  
17 because of repairs and/or improvements made to those assets, but he  
does not know what repairs have been made and he does not have  
any documentation of such repairs.<sup>113</sup>
- 18 • Mr. Rowell did not determine RCND for the Trust assets.<sup>114</sup>

19  
20 <sup>107</sup> Tr. I at 116:6-7 (M. Rowell).

21 <sup>108</sup> Tr. I at 166:19-107:19 (M. Rowell); Tr. I at 169:15-170:7 (M. Rowell).

22 <sup>109</sup> Tr. I at 118:24-119:2 (M. Rowell).

23 <sup>110</sup> Tr. I at 119:2-3 (M. Rowell).

24 <sup>111</sup> Tr. I at 119:6-13 (M. Rowell).

25 <sup>112</sup> Tr. I at 78:10-16 (S. Rowell).

26 <sup>113</sup> Tr. I at 169:15-170:7, at 121:1-10 (M. Rowell).

<sup>114</sup> Tr. I at 122:3-25 (M. Rowell). Under A.A.C. R14-2-103(A)(3)(n), “Reconstructed  
Cost New (RCND) Rate Base” is defined as “an amount consisting of the depreciated  
reconstruction cost new of the property (exclusive of contributions and/or advances in aid  
of construction) at the end of the test year....”.

- 1 • Mr. Rowell does not know what repairs were done to the Hackberry  
2 Transmission Line and he does not know how much those repairs  
cost.<sup>115</sup>
- 3 • Mr. Rowell did not make any inquiries with the Trust relating to  
4 depreciation of the Trust assets.<sup>116</sup>
- 5 • Mr. Rowell did not obtain any documentation from the Trust relating  
6 to the condition, depreciation or original costs of the Trust assets.<sup>117</sup>

7 For regulatory purposes, the value of the Trust assets is based on a net book value  
8 of zero, as dictated by the NARUC Guidelines and Uniform System of Accounts. Put  
9 simply, the NARUC guidelines and accounting standards require that the value of the  
10 Trust assets, if acquired by Truxton, be booked at zero dollars. The idea that a utility  
11 investor is going to pay \$1.4 million for regulated assets that are booked in rate base by  
12 Truxton at zero dollars and fully depreciated defies common sense. In that scenario, the  
13 purported fair market investor would be paying \$1.4 million for plant that will not earn  
14 any return or depreciation expense. And, even worse, the investor will need to provide  
15 additional funding to repair and/or replace those assets in the near future given their  
16 current aged and deteriorated condition.

17 At hearing, Truxton's witnesses focused on the replacement costs of the  
18 transmission lines and the wells, but they did not address the fact that the Trust and  
19 Truxton did not invest in ongoing upgrades or improvements to the system over the years.  
20 Not only did the Trust not invest in improvements and upgrades to the infrastructure, but  
21 the Trust used that system to provide irrigation water to VVPOA for many years, in turn,  
22 siphoning off a substantial amount of revenue from VVPOA since the 1970s.  
23 Commission Staff previously suggested that the Trust violated Commission regulations  
24 by selling water to VVPOA without a CC&N and within Truxton's service territory. As

25 <sup>115</sup> Tr. I at 119:14-120:3 (M. Rowell).

26 <sup>116</sup> Tr. I at 122:18-25 (M. Rowell).

<sup>117</sup> Tr. I at 128:8-10 (M. Rowell).

1 stated by Mr. Stewart, VVPOA paid the Trust in excess of approximately \$2,000,000  
2 since 2002, not including the prior years.<sup>118</sup> To say the least, it is a “double billing” for  
3 the Trust to receive millions in revenue from VVPOA and now seek to include the costs  
4 for transferring that infrastructure to Truxton in VVPOA’s rates.<sup>119</sup> The Trust has  
5 already profited for years from this system and the Commission should not allow the  
6 Trust and Truxton to fabricate another level of affiliate profit for the Trust.

7 That is especially true for VVPOA given that Truxton has not provided adequate  
8 water service to VVPOA on several occasions. In 2011, VVPOA went 30 days without  
9 watering the course due to Truxton breakdowns. It has taken nearly two years for the golf  
10 course to recover.<sup>120</sup> In July 2011, two of the Trust’s wells in the Hackberry Well Field  
11 and the Hualapai 1 Well, which is used to provide sufficient or adequate water service to  
12 VVPOA during the summer, failed and went out of service.<sup>121</sup> Truxton and the Trust  
13 again failed to provide water to VVPOA from September 2-7, 2011 (the Hualapai 1 Well  
14 went out of service again). Additionally, VVPOA was without adequate water service for  
15 a total of 23 days in 2012, including one stretch of 10 days straight and for 29 days in  
16 2013.<sup>122</sup> At hearing, Mr. Neal testified that there is a 75% chance that Truxton will not  
17 be able to provide adequate water service to VVPOA again this coming summer.<sup>123</sup>

18 **V. VVPOA SUPPORTS TRUXTON’S REQUEST FOR FINANCING**  
19 **APPROVAL TO UPGRADE THE HUALAPAI WELL.**

20 At hearing, Mr. Neal proposed that the Commission approve \$127,000 in financing  
21 to convert the Hualapai 1 Well from natural gas to electric service.<sup>124</sup> The evidence

22 <sup>118</sup> Ex. I-5, Stewart RT at 6.

23 <sup>119</sup> Ex. I-5, Stewart RT at 6-7.

24 <sup>120</sup> Ex. I-5, Stewart RT at 7-8.

25 <sup>121</sup> Ex. I-5, Stewart RT at 7.

26 <sup>122</sup> Ex. I-5, Stewart RT at 7-8.

<sup>123</sup> Tr. II at 247:5-10 (Neal).

<sup>124</sup> Tr. II at 257:9-13, 284:16-20 (Neal).

1 shows that such upgrade will make the Hualapai 1 Well more reliable and less costly to  
2 operate. VVPOA supports Truxton's request for financing approval to upgrade the  
3 Hualapai 1 Well from natural gas to electric service. As testified by Mr. Stewart,  
4 VVPOA is "in agreement with that changeover, as long as the costs that are passed on to  
5 [VVPOA] are reasonable and we can afford them."<sup>125</sup>

6 Mr. Neal testified that failure of the Hualapai 1 Well this summer would result in  
7 "catastrophic" circumstances for VVPOA and that the "golf course is going to die."<sup>126</sup>  
8 The Hackberry well field provides adequate service to VVPOA and residential customers  
9 during the winter months and "it's a very inexpensive system to run because it's gravity  
10 fed, and the wells are shallower so it works pretty well in the winter."<sup>127</sup> During the  
11 summer months, however, the Hackberry system does not provide enough water to serve  
12 VVPOA and residential customers, necessitating use of the Hualapai 1 Well. The  
13 Hualapai 1 Well is 1,000 feet deep and powered by two Caterpillar natural gas engines  
14 that are old and difficult to repair.<sup>128</sup> According to Mr. Neal, "there's a 75 percent change  
15 that one of those two engines will fail before August [2014]."<sup>129</sup> For that reason, the  
16 Commission should authorize Truxton to obtain the necessary financing to upgrade the  
17 Hualapai 1 Well as soon as possible.

18 **VI. VVPOA'S RATES SHOULD NOT INCLUDE ANY CHARGES RELATING**  
19 **TO ARSENIC TREATMENT.**

20 Truxton seeks Commission approval for \$1,819,208 in financing for the cost of  
21 acquiring and installing plant to treat and blend water to resolve arsenic compliance  
22 issues, along with the acquisition of wells and transmission lines currently owned by the  
23

24 <sup>125</sup> Tr. II at 403:4-7 (Stewart).

25 <sup>126</sup> Tr. II at 243:17-244:3 (Neal).

26 <sup>127</sup> Tr. II at 245:2-12 (Neal).

<sup>128</sup> Tr. II at 245:18-25 (Neal).

<sup>129</sup> Tr. II at 247:5-10 (Neal).

1 Neal Family Trust. As stated by Mr. Neal, the proposed financing amount for the ATF is  
2 \$193,000.<sup>130</sup> VVPOA supports Truxton's attempts to build an arsenic treatment system  
3 and believes such system is in the public interest of Truxton's customers. Even so,  
4 arsenic treatment is not necessary for the non-potable water service provided to  
5 VVPOA.<sup>131</sup> The arsenic levels do not directly affect irrigation of the golf course.

6 With respect to arsenic treatment, VVPOA does not believe it should pay for the  
7 costs of arsenic treatment. VVPOA uses bulk irrigation water. As a result, it is not fair  
8 for VVPOA to pay for arsenic treatment when VVPOA is using non-potable irrigation  
9 water. On page 4 of his rebuttal testimony, Mr. Neal states that "[t]he Company also  
10 understands there is no need to treat arsenic for irrigation. But the cost of the  
11 improvements will then fall upon the other customers."<sup>132</sup> Of course, the costs for such  
12 facilities should be borne by the customers that use and benefit from such facilities.

13 All things considered, VVPOA supports Truxton's request to finance construction  
14 of an ATF, but the evidence demonstrates that VVPOA's rates for irrigation water should  
15 not include any charges associated with arsenic treatment. Commission Staff, Truxton  
16 and VVPOA all agree that arsenic treatment is not necessary for the non-potable,  
17 irrigation water sold to VVPOA. VVPOA acknowledges that its potable water rates may  
18 include charges for the ATF, but VVPOA's irrigation rates should not include any  
19 charges associated with the ATF.

20 **VII. ADDITIONAL LEGAL ISSUES.**

21 At hearing, the Administrative Law Judge ("ALJ") requested the parties "to brief  
22 whether or not the Trust is acting as a public service corporation in the CC&N area."<sup>133</sup>  
23

24 <sup>130</sup> Tr. II at 284:6-11 (Neal).

25 <sup>131</sup> Ex. I-4, Stewart DT at 15-16; Ex. I-5, Stewart RT at 4.

26 <sup>132</sup> Ex. A-5, Neal RT at 4; Tr. II at 298:19-299:3 (Neal).

<sup>133</sup> Tr. III at 659:14-17 (ALJ Kinsey).

1 Generally speaking, VVPOA does not believe there is sufficient evidence in the record to  
2 determine whether the Trust is acting as a “public service corporation” (PSC) under  
3 Arizona law, primarily because no witness testified on behalf of the Trust.

4 Article 15, § 2 of the Arizona Constitution defines a water PSC as: “All  
5 corporations other than municipal engaged in ... furnishing water for irrigation, fire  
6 protection or other public purposes.” As noted in the previous OSC proceeding, the  
7 record indicated that the Trust previously acted as a PSC by selling water to VVPOA  
8 within Truxton’s CC&N and using the same utility facilities as Truxton. Under Decision  
9 No. 72386, VVPOA became a customer of Truxton and VVPOA does not know whether  
10 the Trust is continuing to sell water to any other entities within Truxton’s CC&N.

11 Aside from the question of whether the Trust is acting as a PSC, there is evidence  
12 in the record supporting the legal conclusion that the Trust and Truxton may be alter egos.  
13 That inquiry may be relevant to the extent the Trust continues to condition its transfer of  
14 the Trust assets to Truxton on payment of \$1.4 million. Under *Gatecliff v. Great Rep.*  
15 *Life Ins. Co.*, 170 Ariz. 34, 38, 821 P.2d 725, 729 (1991), it is “well settled law that a  
16 corporation is a separate legal entity.” Generally, Arizona courts use a two-pronged test  
17 to determine whether a party falls under an alter ego theory. The party alleging alter ego  
18 status “must prove both (1) unity of control, and (2) that observance of the corporate form  
19 would sanction fraud or promote injustice.”<sup>134</sup>

20 Here, there is evidence of common officers and directors between the Trust and  
21 Truxton, payment of expenses of Truxton by the Trust, comingled funds, uses of the same  
22 water facilities and assets, and other factors indicating unity of control. That’s not to  
23 mention that when Truxton was formed as a regulated utility in 1971-1972, the Neal  
24 Family opted to retain ownership of the water facilities in the family trust, further

25  
26 <sup>134</sup> *Gatecliff*, 170 Ariz. at 37, 821 P.2d at 728.

1 indicating unity of control between the Trust and Truxton. To extent there is unity of  
2 control, the Commission may be inclined to treat the Trust and Truxton as the same entity.

3 Here, there also is evidence supporting a legal conclusion that the Trust retained  
4 ownership of the Trust assets in constructive trust for Truxton in providing water service  
5 to customers. The imposition of a constructive trust is an equitable remedy that arises by  
6 operation of law to prevent one person from being unjustly enriched at the expense of  
7 another.<sup>135</sup> “A court may impose a constructive trust whenever title to property has been  
8 obtained through actual fraud, misrepresentation, concealment, undue influence, duress or  
9 through any other means which render it unconscionable for the holder of legal title to  
10 continue to retain and enjoy its beneficial interest.”<sup>136</sup>

11 At hearing, Mr. Neal testified that when Truxton was formed in 1972, the Trust  
12 opted to maintain ownership of the assets necessary and useful for Truxton to provide  
13 water service (including the Hackberry Wells and Hualapai 1 Well) in order to “avoid  
14 going before the ACC and having to deal with all of the regulatory issues.”<sup>137</sup> In essence,  
15 the Trust created the legal problems associated with the Trust assets by attempting to  
16 avoid Commission regulation over use of those assets in the first place. As such, if the  
17 Trust continues its refusal to transfer the Trust assets to Truxton, imposition of a  
18 constructive trust may remedy the issues surrounding the Trust assets.

### 19 **VIII. CONCLUSION**

20 For the reasons noted above, and based on the evidence presented at hearing,  
21 VVPOA requests that the Commission adopt VVPOA’s recommendations above.

24 <sup>135</sup> *Turley v. Ethington*, 213 Ariz. 640, 643, ¶¶ 8–9, 146 P.3d 1282, 1285 (App.2006)  
25 (citations omitted).

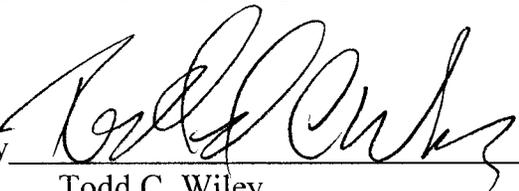
26 <sup>136</sup> *Id.*

<sup>137</sup> Tr. Vol. II at 269:15-270:18 (Neal).

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Dated: April 25, 2014

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1 ORIGINAL and 13 copies  
2 of the foregoing was filed  
3 this 25<sup>th</sup> day of April, 2014,  
4 with:

5 Docket Control  
6 Arizona Corporation Commission  
7 1200 West Washington Street  
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9 COPY of the foregoing  
10 was hand-delivered this  
11 25<sup>th</sup> day of April, 2014, to:

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