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MEMORANDUM
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TO: Docket Control Center

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THRU: Steven M. Olea
Director
Utilities Division

AZ CORP COMMISSION
DOCKET CONTROL

DATE: February 10, 2011

RE: STATUS REPORT ON MONTEZUMA RIMROCK WATER CO., LLC (DOCKET NOS. W-04254A-08-0361 AND W-04254A-08-0362)

Purpose

On December 11, 2009, Montezuma Rimrock filed for an extension of time until June 30, 2010, for the provision of the Well #4 Approval of Construction ("AOC"). The Company identified that the rationale behind the request was found in the processing of the item at the ADEQ as ADEQ had informed MRWC that "an AOC will not be granted until the installation of the Arsenic Treatment System is complete". This prevented the Company from obtaining the Well #4 AOC prior to the original December 31, 2009 due date. The purpose of this memorandum is to provide the Commission with updated information.

Background

In Decision No. 71317, dated October 30, 2009, the Commission approved the application of Montezuma Rimrock for approval of a rate increase and financing. As part of Decision No. 71317, the Commission ordered the following:

"...Montezuma Rimrock Water Company, LLC shall file with Docket Control, as a compliance item in this Docket, by December 31, 2009 a copy of the Arizona Department of Environmental Quality Certificate of Approval of Construction for the new Well #4."

Staff confirmed with ADEQ that approval of the Arsenic Treatment System was a prerequisite to receipt of an AOC for Well # 4. Staff further found that the water quality of Well #4 did not meet drinking water standards and would not meet such standards without the installation of an arsenic treatment system. Therefore, Staff did not object to Montezuma Rimrock's request for an extension of time until June 30, 2010 to provide the AOC related to Well #4.

ROO / Open Meeting

On February 11, 2010, the Hearing Division issued a Recommended Opinion and Order which approved Montezuma Rimrock's request for extension of time until June 30, 2010, for provision of the ADEQ AOC. However, at the March 2, 2010 Open Meeting, the discussion centered on a citizen complaint over an environmental concern which had not arisen during the original Water Infrastructure Finance Authority ("WIFA") loan application review.

The citizen complaint alleged that the distance between a Company well (Well #4) and the Montezuma National Park Monument was sufficiently short as to constitute an "environmental" issue. This monument is a part of, and is encompassed by, Montezuma National Park which is within the United States National Park Service. The fact that the complaint was filed lead to the question of whether a Categorical Exemption ("CE") was warranted for the Montezuma arsenic treatment project.

A CE is an identified type of action or project which does not now, or over time, have a significant effect on the quality of the human environment. It involves the review and analysis of Company supplied environmental information and culminates in an administrative stamp or condition stating that the scope of a project is so minor that it has been categorized as a project that does not need a full environmental review.

WIFA / NEPA

As a State agency authorized to dispense federal funds, WIFA is responsible for meeting requirements of the National Environmental Policy ACT ("NEPA"). For detail on NEPA, the United States Environmental Protection Agency's ("US EPA") website provides the following:

"NEPA requires federal agencies to integrate environmental values into their decision making processes by considering the environmental impacts of their proposed actions and reasonable alternatives to those actions."

"To meet NEPA requirements federal agencies prepare a detailed statement known as an Environmental Impact Statement ("EIS"). EPA reviews and comments on EIS's prepared by other federal agencies, maintains a national filing system for all EIS's, and assures that its own actions comply with NEPA"

In WIFA's case, a categorical exemption was originally granted to the Montezuma Rimrock arsenic treatment project based on information provided by the Company. Without a CE, WIFA would likely be required to conduct additional environmental research on the Montezuma project in order to comply with NEPA standards. Such further research could lead to WIFA determining that a Finding of No Significant Impact ("FONSI") is warranted or, more stringently, that a full bore environmental review is necessary. A full review would lead to the issuance of the more detailed and formal Environmental Impact Statement ("EIS").

WIFA Action

The customer complaint highlighted the question of whether the CE was appropriately granted to Montezuma Rimrock. Indeed, on February 3, 2010, Ms. Sara Konrad, an Environmental Program Specialist at WIFA, sent an e-mail to Ms. Patsy Olsen of the Company stating that:

"the Categorical Exemption previously issued for this project may not have been warranted as WIFA has recently received information that the project does not qualify under one or more of the categories in R18-15-107 (B)."

“WIFA must further verify conditions surrounding this project. To do so, you will need to prepare an Environmental Information Document (EID).”

“If it so happens that these issues are not significant, then WIFA can, upon receipt of the EID, issue a Finding of No Significant Impact (FONSI). At that point, WIFA will publicly notice the FONSI for a period of 30 calendar days and receive and review any comments. If these issues are significant, then an Environmental Impact Statement will be required, and WIFA will contact you about proceeding with that process.”

Montezuma Rimrock was therefore required to produce an EID presenting pertinent environmental information for review by WIFA or its designee.

The EID

On September 9, 2010, Montezuma Rimrock provided Staff a copy of the EID prepared by the Company. Ms. Konrad of WIFA stated that the analysis and review of the EID would be completed and WIFA would then present its findings. The EID was therefore provided to WIFA’s consultant, AZTEC Engineering, for its engineering and technical review. The Environmental Protection Agency (“EPA”) was also reviewing the document.

On November 18, 2010, AZTEC Engineering provided WIFA with its “Environmental Review and Recommendations” on the EID and ultimately recommended that “WIFA consider completing an Environmental Impact Statement” (“EIS”). The Environmental Protection Agency (“EPA”) made the same recommendation to WIFA.

The EIS

WIFA elected to accept and implement the recommendation of Aztec Engineering and the EPA to require a full bore environmental review relating to Montezuma Rimrock. As such, on November 22, 2010, WIFA notified the Company that, as a result of its investigation, “an Environmental Impact Statement (EIS) will be required for this project to receive WIFA funding.”

When Staff inquired, Ms. Konrad stated that the EIS process would be a much more difficult and costly one than the more simplistic EID which the Company has already prepared. It is possible that the EIS process could more than double the cost of the loan and take many months to reach a conclusion.

Montezuma Rimrock now has a decision on whether to continue pursuing the pending WIFA loan. Given the anticipated depth and cost of the EIS process, it is expected that the Company will decide that continued participation in the process is not viable for a company its size. That decision had been expected relatively soon. WIFA’s November 22, 2010, letter gave Montezuma Rimrock until December 31, 2010, to notify the agency if the Company would continue to pursue WIFA funding for the arsenic project. However, in a January 5, 2011 discussion with WIFA, Ms. Sara Konrad stated that Montezuma Rimrock requested and received an extension until

January 31, 2011, to communicate its intention to pursue the WIFA funding. **Further, as this is the first time WIFA has ever required an EIS, it is difficult to predict how the process would unfold if the Company elects to continue to pursue the WIFA loan.**

Company Performance

On December 16, 2010, Staff contacted both WIFA and ADEQ to inquire about Montezuma's requirements and level of cooperation with those agencies.

Ms. Konrad stated that the Company had been cooperative in its dealings with WIFA. Ms. Vivian Burns at ADEQ stated that the Company had cooperated 100 percent with that agency and was now providing drinking water from a reverse osmosis system in the Company's offices.

Further, Montezuma Rimrock is not currently out of compliance with ADEQ regarding the installation of the arsenic treatment system as the June 7, 2010, consent order provides the Company with one year to complete the construction of the arsenic treatment system and submit the application for AOC. Montezuma therefore may not be out of compliance in that regard until June 7, 2011.

Company Intention

Finally, the Company has had several discussions with Staff in which it inquired about its remaining options. Staff told the Company it could either continue to pursue the WIFA loan by participating in the EIS or seek to modify the decision that ordered the loan through WIFA.

As the Company demonstrated an interest in modifying the decision to take the loan from another entity, Staff advised the Company of its option to file requesting an A.R.S. §40-252 to modify the existing decision. The Company subsequently indicated to Staff its intent to request an amendment to Decision No. 71317 which would seek approval to utilize another lender. As shown below, Decision No. 71317 currently provides that the loan be taken only from WIFA:

"It is further ordered that Montezuma Rimrock Water Company, LLC is hereby authorized to incur long-term debt in the form of a Water Infrastructure Finance Authority of Arizona loan in an amount up to \$165,000, with a term of 20 years and on such terms and interest rates as are prevailing at the time the Water Infrastructure Finance Authority approves the loan."

Summary

As discussed at Open Meeting, the Commission ordered the provision of AOC's on the arsenic treatment and Well #4 construction projects. Given the overall cooperation of Montezuma Rimrock with State agencies, Staff concludes that the Company is seriously attempting to fulfill its arsenic treatment mandate to comply with ADEQ and the Commission, therefore, Staff is not recommending any action at this time. The Company is demonstrating a good faith effort and has been notified by Staff of its option to pursue an amendment to the Commission decision. An

amendment could allow the Company to obtain the loan from an entity other than WIFA, which may negate the need for an EIS thereby providing substantial savings for ratepayers.

On January 24, 2011, the Company made a formal filing, per A.R.S. §40-252, requesting that Decision No. 71317 be amended to allow the Company to seek the funding from a private financial institution. This request is currently pending possible Commission action.

SMO: BKB:lm

Originator: Brian K. Bozzo

SERVICE LIST FOR:
DOCKET NOS.

MONTEZUMA RIMROCK WAER CO., LLC.
W-04254A-08-0361 & W-04254A-08-0362

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