

JIM IRVIN  
COMMISSIONER-CHAIRMAN  
TONY WEST  
COMMISSIONER  
CARL J. KUNASEK  
COMMISSIONER



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STUART R. BRACKNEY  
ACTING EXECUTIVE SECRETARY

ARIZONA CORPORATION COMMISSION

DATE: APRIL 20, 1999  
DOCKET NO: WS-03478A-98-0650  
TO ALL PARTIES:

Enclosed please find the recommendation of Hearing Officer Jane Rodda. The recommendation has been filed in the form of an Order on:

FAR WEST WATER & SEWER, INC.  
(FINANCING)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Hearing Officer by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

APRIL 29, 1999

The enclosed is NOT an order of the Commission, but a recommendation of the Hearing Officer to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

MAY 11, 1999 and MAY 12, 1999

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250.

  
STUART R. BRACKNEY  
ACTING EXECUTIVE SECRETARY

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 JIM IRVIN  
COMMISSIONER-CHAIRMAN  
3 TONY WEST  
COMMISSIONER  
4 CARL J. KUNASEK  
COMMISSIONER  
5

6 IN THE MATTER OF THE APPLICATION OF  
FAR WEST WATER & SEWER, INC., AN  
7 ARIZONA CORPORATION, FOR AUTHORITY  
TO (1) INCUR LONG-TERM INDEBTEDNESS IN  
8 THE AMOUNT OF \$6,000,000 AND (2) INCUR  
SHORT-TERM INDEBTEDNESS RELATING TO  
9 THE CONSTRUCTION OF UTILITY PLANT AND  
IMPROVMENTS TO ITS SYSTEM.

DOCKET NO. WS-03478A-98-0650

DECISION NO. \_\_\_\_\_

**ORDER**

10 Open Meeting  
11 May 11 and 12, 1999  
12 Phoenix, Arizona

13 **BY THE COMMISSION:**

14 On November 2, 1998, Far West Water & Sewer, Inc. ("Far West" or "Company") filed an  
15 application with the Arizona Corporation Commission ("Commission") requesting authority to incur  
16 long-term debt in the amount of \$6.0 million and to incur short-term debt in the amount of \$5.0  
17 million. The Company intends to use the debt proceeds to finance the purchase and installation of  
18 utility plant.

19 On January 29, 1999, the Commission's Utilities Division Staff ("Staff") filed a Staff Report  
20 in this matter. Staff recommended that the Commission approve the Company's financing request.

21 Background

22 Far West provides water utility service to approximately 9,000 customers in an area located  
23 near the City of Yuma, Arizona. The Commission approved Far West's current rates in Decision No.  
24 60437 (September 29, 1997).

25 Far West's water supply contains high levels of total dissolved solids ("TDS"). Over the  
26 years, the Commission's Consumer Services Section has received numerous complaints about the  
27 appearance, taste and corrosiveness of Far West's water. At the public comment session held in  
28 conjunction with the Company's last rate application, on April 1, 1997, the vast majority of

1 comments were about the quality of the water. In Decision No. 60437, the Commission ordered Far  
2 West to perform a study of its water quality problems, addressing in particular, ways to efficiently  
3 and cost-effectively meet customer expectations for safe and potable water.

4 The Company filed a report with the Commission's Utilities Division, as required in Decision  
5 No. 60437, in which the Company's engineers and consultants discussed various alternatives. The  
6 Company concluded that its best alternative to alleviate the TDS problem is to acquire a source of  
7 Colorado River water and construct water treatment and delivery facilities. Far West has contracted  
8 with the Yuma Mesa Irrigation Drainage District (the "District") to purchase up to 5,000 acre-feet of  
9 Colorado River water annually.<sup>1</sup> Far West determined that the option to construct a 4.0 million  
10 gallon per day treatment plant and related transmission mains and pumping facilities was the best  
11 alternative. This option would give the Company the greatest flexibility and the lowest initial capital  
12 cost.

13 In its application, the Company reported that it had already completed the 20-inch  
14 transmission main that will be used to transport raw Colorado River water from the District's canal to  
15 the location of the treatment plant. In addition, the Company has incurred preliminary costs for  
16 engineering and design work and for the purchase of materials. The Company's goal is to complete  
17 construction of the treatment plant in July 1999.

#### 18 Financing Request

19 The total estimated cost of the project is \$7.2 million. The Company expects to complete the  
20 project for \$6.0 million based upon its experience in the early stages of construction. If the costs  
21 exceed \$6.0 million, the Company will finance the additional amounts with paid-in capital.

22 Staff's Engineering Report, filed as part of the Staff Report, also analyzes the Company's  
23 alternatives, and concurs with the Company's choice. Staff believes that the Company's chosen  
24 option is a reasonable solution to the water quality problems and that the cost estimates are also  
25 reasonable. Staff noted that the surface water treatment plant will markedly improve, but not  
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28 <sup>1</sup> In the future, the Company could potentially purchase an additional 5,000 acre feet of water annually.

1 eliminate, the salinity of the water delivered to users, however, it should eliminate the iron and  
2 manganese problems.

3 The Company is requesting approval to borrow \$5.0 million in short-term debt as interim  
4 construction financing. The Company would borrow this money from H&S Developers, Inc.  
5 ("H&S"), Far West's stockholder. Accrued interest and the principal balance on the H&S loan are  
6 due on May 15, 1999. The interest rate is prime plus 1.5 percent (based on a current prime of 7.75  
7 percent, the interest rate is 9.25 percent). The Company plans to replace this short-term loan with  
8 long-term debt. At the time of the Staff Report, the Company was finalizing the terms and conditions  
9 of a loan with Capital Bank for a 20 year loan at an interest rate of 8.0 percent. The Company may  
10 have to pay a loan origination fee of 0.75 to 1.0 percent. Annual payments on such a loan would be  
11 \$611,000.

12 Financial Impact

13 Staff has analyzed the financial impact of the proposed debt, the plant additions and the cost  
14 of purchasing water from the District. In 1997, Far West had no debt and consequently, no  
15 meaningful Times Interest Earned Ratio ("TIER") or Debt Service Coverage ratio ("DSC"). Based  
16 on 1997 revenues, the additional principal and interest associated with the \$6.0 million debt would  
17 result in a TIER of -0.29 and a DSC of 0.3. Thus, based on 1997 figures, the Company had  
18 insufficient operating income to make its expected debt payments. The substantial increase in rate  
19 base as a result of the new plant and added expense of the purchasing water from the District may  
20 have a significant impact on rates, although the ultimate effect won't be known until the Company's  
21 next rate case.<sup>2</sup>

22 Compliance Issues

23 The Arizona Department of Environmental Quality ("ADEQ") reported that Far West is in  
24 substantial compliance with drinking water rules and regulations with some deficiencies. Because  
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26 <sup>2</sup> The Company filed a permanent rate case on February 10, 1999 (Docket No. WS-03478A-99-0144). Staff's  
27 analysis based on a weighted cost of capital of 9.1 percent, indicates Far West's ratepayers would experience an  
28 approximate increase of \$11.65 per month. Staff's estimate of the effect on rates does not include such factors as the  
effect of income tax expense or customer growth or other items that might have changed since the last rate case. The  
Company also filed an interim rate case on April 9, 1999 which proposed an average monthly increase for residential  
customers of \$8.53.

1 the deficiencies involved monitoring, ADEQ would not state that the Company is meeting the Safe  
2 Drinking Water Act water quality standards.

3 The Company is current in its property tax payments.

4 Recommendations

5 Staff recommends approval of the financing request because the proposed plant additions are  
6 a reasonable and cost-effective resolution of the Company's water quality problems. Staff  
7 recognized that the effect on rates may be significant, but believed that customer interest in the water  
8 quality problem is strong. Staff believed that the benefits of the proposed project are substantial and  
9 should not be delayed. However, Staff also recommended that the Company complete the required  
10 monitoring to the satisfaction of ADEQ as soon as possible so that ADEQ can confirm that Far West  
11 is delivering water that has no maximum contaminant level violations and meets the standards of the  
12 Safe Drinking Water Act. Staff recommended that such confirmation be received by the Director of  
13 the Utilities Division by December 31, 1999, or Staff should recommend that the Commission issue  
14 an Order to Show Cause requiring Far West to show why a fine or other penalty should not be  
15 imposed.

16 We concur with Staff's recommendations. The water quality issue is a serious one for this  
17 Company and in its last rate case, the Commission ordered the Company to find a way to ameliorate  
18 the problem. While it appears the proposed solution may have a substantial affect on rates, we note  
19 that current rates are relatively low<sup>3</sup> and that customers could see savings as the water's corrosiveness  
20 is improved.

21 \* \* \* \* \*

22 Having considered the entire record herein and being fully advised in the premises, the  
23 Commission finds, concludes, and orders that:

24 FINDINGS OF FACT

25 1. Far West is an Arizona corporation that provides water utility service to approximately  
26 9,000 customers in an area near Yuma, Arizona.

27  
28 <sup>3</sup> Currently, 5/8" x 3/4" meter customers pay a monthly minimum of \$6.00 and \$0.7699 per 1,000 gallons.

1           2.       On November 10, 1998, Far West filed an application with the Commission  
2 requesting authority to incur short-term debt of \$5.0 million and to incur long-term debt of \$6.0  
3 million.

4           3.       The debt proceeds would be used to finance the construction of a 4.0 million gallon per  
5 day water treatment plant along with related pumping stations, transmission mains and storage to  
6 treat Colorado River water.

7           4.       The Company's current ground water supply contains high TDS which have caused  
8 Far West's customers to complain about the taste and corrosive damage to appliances.

9           5.       In Decision No. 60437, the Commission ordered Far West to conduct a study of  
10 possible solutions to its water quality problem.

11          6.       The Company has determined that the most reasonable solution is to purchase  
12 Colorado River water from the District and blend it with its ground water sources.

13          7.       The acquisition of surface water requires the Company to construct a water treatment  
14 plant and related facilities.

15          8.       Far West plans to borrow \$5.0 million in short-term funds on an interim basis from its  
16 parent company, H&S, and thence to replace the short-term debt with \$6.0 million in long-term debt  
17 from an independent lender.

18          9.       Far West expects to be able to obtain a 20 year \$6.0 million loan at an interest rate of  
19 8.0 percent annually.

20          10.      On January 29, 1999, Staff filed a Staff Report in this matter in which Staff  
21 recommended that the financing request be granted.

22          11.      Engineering Staff reviewed the project to be financed and found it to be a reasonable  
23 resolution of the water quality issues and that the cost estimates were reasonable.

24          12.      Far West is current in the payment of property taxes.

25          13.      Although ADEQ reports the Company to be in substantial compliance with its rules  
26 and regulations, ADEQ cannot determine if Far West is providing water that meets the quality  
27 standards of the Safe Drinking Water Act because the Company has monitoring deficiencies.  
28



1 IT IS FURTHER ORDERED that such authority is expressly contingent upon Far West Water  
2 and Sewer, Inc.'s use of the proceeds for the purposes set forth in its application.

3 IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not  
4 constitute or imply approval or disapproval by the Commission of any particular expenditure of the  
5 proceeds derived thereby for purposes of establishing just and reasonable rates.

6 IT IS FURTHER ORDERED that Far West Water and Sewer, Inc. shall file with the Director  
7 of the Utilities Division evidence that it is delivering water that meets the water quality standards of  
8 the Safe Drinking Water Act by December 31, 1999. In the event Far West Water and Sewer, Inc.  
9 fails to comply, Staff shall recommend to the Commission whether to issue an Order to Show Cause  
10 why fines and penalties should not be imposed.

11 IT IS FURTHER ORDERED that Far West Water and Sewer, Inc. shall file copies of all  
12 executed financing documents setting forth the terms of the financing, within 30 days of obtaining  
13 such financing.

14 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

15 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

16  
17 \_\_\_\_\_  
COMMISSIONER-CHAIRMAN      COMMISSIONER      COMMISSIONER

18  
19 IN WITNESS WHEREOF, I, STUART R. BRACKNEY,  
20 Acting Executive Secretary of the Arizona Corporation  
21 Commission, have hereunto set my hand and caused the official  
22 seal of the Commission to be affixed at the Capitol, in the City  
23 of Phoenix, this      day of      , 1999.

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25 STUART R. BRACKNEY  
26 ACTING EXECUTIVE SECRETARY

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1 SERVICE LIST FOR: FAR WEST WATER AND SEWER, INC.

2 DOCKET NO.: WS-03478A-98-0650

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10 Paul Bullis, Chief Counsel  
11 Legal Division  
12 ARIZONA CORPORATION COMMISSION  
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15 Director, Utilities Division  
16 ARIZONA CORPORATION COMMISSION  
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