

DECISION MEMORANDUM

**TO: COMMISSIONER KJELLANDER
COMMISSIONER SMITH
COMMISSIONER HANSEN
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL**

FROM: JOHN R. HAMMOND

DATE: MAY 24, 2004

RE: IN THE MATTER OF THE APPLICATION OF CDS STONERIDGE UTILITIES, LLC TO AMEND ITS CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO INTERCONNECT WITH AND ACQUIRE THE SERVICE TERRITORY OF HAPPY VALLEY RANCHOS, INC. AND TO IMPLEMENT A SURCHARGE, CASE NO. SWS-W-03-1.

On May 21, 2004, the Commission Staff received information from the Division of Environmental Quality and the engineering firm employed by CDS Stoneridge Utilities LLC indicating that Final Order No. 29320 would have to be amended to authorize the Company to borrow additional funds to complete the interconnection project and additional system upgrades.

BACKGROUND

On August 26, 2003, the Commission by its Order No. 29320 authorized Stoneridge to borrow \$213,450 from the State Water Quality revolving fund (DEQ) at a 2% interest rate. The purpose of the loan is to provide an interconnection between and combine Stoneridge with the Happy Valley Rancho's Homeowners Association system. The Order authorized a surcharge of \$12.65, subject to true-up, to be applied only to the customers on the Happy Valley Rancho's portion of the system to repay the low interest loan. The Happy Valley Rancho's existing water quality is poor and interconnection with Stoneridge as a combined system is the best solution to the problem.

1. Request for Additional Borrowing Authority for the Interconnection Project

Staff has been informed that several factors have escalated the estimated construction cost: a) the State Historical Preservation Office required an archeological study be performed to determine if there were cultural resources that would be impacted by the construction project. This

study added \$4,000 to the project cost; b) an additional easement was required that was not initially identified. The cost of the easement added \$4,000 to the cost of the project; and c) the original construction cost estimate of \$167,550 was prepared in May 2003. Bids have been received from contractors. The lowest qualifying bid is \$182,990 representing an increase above the estimate of approximately 10.8%. This bid is only good for ten (10) days and expires today May 24, 2004. According to Sewell Engineers, the reason for the short bid window is notice from the bidder that the material suppliers were unwilling to lock in prices that are escalating rapidly. The price escalation is due mostly to the cost of petroleum products used in the manufacture and transportation of the materials.

The total cost of the project with these changes is \$235,990 rather than the original cost estimate approved by the Commission of \$213,450. Stoneridge Utilities and the Department of Environmental quality would like the Commission to approve the additional loan amount expeditiously.

Staff Recommendation

Staff believes the cost is reasonable and in the best interest of the customers on the Happy Valley Ranchos part of the system and recommends the Commission grant the Company the authority to borrow the additional loan funds. Staff also believes that the additional funds should be recovered through the same surcharge mechanism approved by the Commission in Order No. 29320. Initially, the surcharge was set at \$12.65, subject to true-up, for 20 years for HVR customers and any customer joining the system downstream of the interconnection point between the HVR and Stoneridge systems. Order No. 29320 at 9. With these new amounts the surcharge will have to be adjusted and Staff recommends that the Commission reserve judgment on the appropriate amount of the surcharge until the State Drinking Water Revolving Fund Loan is finalized and disbursed and the construction costs are more certain.

2. Request for Additional Borrowing Authority to make Water System Improvements

During the on-going review process, the Department of Environmental Quality has identified additional improvement to the system that the Department desires be made to bring the system into full compliance with the "Ten State Standards" that all water utilities will be required to meet. These additional improvements include automated controls and alarms on the Stoneridge wells and reservoirs to alert the operators of problems before they become so severe that water

supply is interrupted to customers. The preliminary estimated costs of these improvements are \$88,000. No detailed engineering has been performed at this time. These improvements are not tied directly to the acquisition of the Happy Valley Ranchos part of the system. These improvements would be required either with or without this acquisition and therefore are a backbone system improvement to benefit all customers.

The Department of Environmental Quality is willing to include the cost of the additional backbone improvements in the low interest 2% loan authorized to integrate the Happy Valley Ranchos into the Stoneridge system. If these costs are not included in this loan, Stoneridge may be required to seek capital elsewhere at a higher cost.

Staff Recommendation

Staff believes the system controls proposed to be added are a necessary and prudent investment to be made at this time. If the Commission agrees, the total loan authorization will need to be increased from the existing \$213,450 to 323,990. As stated above Staff believes the Commission should increase the authorized surcharge for the Happy Valley customers to pay only for the increased loan service cost of the interconnection project. The loan service costs associated with the backbone improvement should be borne by all customers on the system including the Condominium Association, Golf Course and existing residential customers as well as the new Happy Valley customers that will be added to the system.

Staff recommends approval of the additional borrowing authority but believes the Commission should reserve judgment on how to collect the cost of the backbone improvement project. Either a separate surcharge or an increase in base rates may be appropriate. Staff cannot at this time estimate the effect these costs on the base or an appropriate surcharge without more detailed analysis. The Company should keep the Commission and the Staff apprised of the additional amount borrowed for this backbone improvement once the State Drinking Water Revolving Fund Loan is finalized and the construction/engineering costs as they become more certain. Staff recommends that the Commission direct the Company provide it with this information in a timely manner.

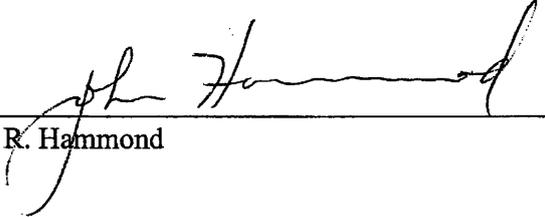
COMMISSION DECISION

1. Does the Commission wish to approve the increase in the original amount of the loan to \$235,990 for the Happy Valley Ranchos acquisition and interconnection project?

2. Does the Commission wish to allow the Company to recover this additional amount through the surcharge mechanism approved in Order No. 29320?

3. Does the Commission wish to approve the additional loan amount of \$88,000 to complete the backbone system improvements required by DEQ?

4. Does the Commission wish to reserve judgment on how to collect the cost of the backbone system improvement project?



John R. Hammond

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