

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: April 10, 2018

REGULAR _____ CONSENT X EFFECTIVE DATE _____ N/A _____

DATE: March 28, 2018

TO: Public Utility Commission

FROM: Malia Brock *MB*

THROUGH: Jason Eisdorfer, Bryan Conway, and Bruce Hellebuyck *ME* *B*

SUBJECT: PELICAN BAY HEIGHTS WATER SYSTEM, LLC.: (Docket No. UP 356)
Requests Approval for the Annexation of Pelican Bay Heights Water System, LLC to Harbor Water People's Utility District.

STAFF RECOMMENDATION:

The Public Utility Commission of Oregon (Commission) should approve the annexation of Pelican Bay Heights Water System, LLC (Pelican Bay or Company) to Harbor Water People's Utility District (Harbor Water) subject to the following conditions:

1. Company shall notify the Commission in advance of any substantive changes to the transfer of properties, including any material changes in price or conditions of service. Any changes to the agreement terms that alter the intent or extent of activities under the agreement from those approved herein shall be submitted for approval in application for a supplemental order (or other appropriate form) in this docket.
2. Pelican Bay will provide notice to the Commission within 10 days of the close of the annexation.

DISCUSSION:

Issue

Whether the Commission should approve the annexation of Pelican Bay to Harbor Water.

Applicable Rule or Law

ORS 757.480(5) and OAR 860-036-2120(1) require water utilities doing business in Oregon to obtain Commission approval prior to disposing of the water utility. The Commission has traditionally applied a public interest “no harm” standard when considering whether or not to approve the transaction.¹

Pursuant to OAR 860-036-2120(4), the utility must provide the Commission and its customers with notice of the annexation or sale no less than 60 days prior to the closing date of the transaction.

Analysis

Background

Pelican Bay is a small investor-owned, rate-regulated water utility located in Harbor, Oregon. Currently the Company provides domestic residential water service to 22 customers, and there are an additional eight undeveloped lots that could potentially be utilized for home sites. Pelican Bay does not have any wells, and presently purchases all of its water from Harbor Water and then pumps the water uphill to the end users. The current owner of the Company acquired the water system upon the death of the previous owner. The current owner wishes to retire.

Harbor Water is a Public Utility District, and not regulated by the Commission. Harbor Water was established in 1962, and started providing water service in 1966. There are 1,677 active customers, the majority of which are residential. Harbor Water provides water service exclusively in the Harbor, Oregon area.

Pelican Bay recently completed the installation of two 10,000 gallon reservoir tanks, including all of the supporting infrastructure, as part of the requirement for the annexation. The Company received Commission approval (UF 4295) in 2015 to secure financing from the Safe Drinking Water Revolving Loan Fund, administered by Business Oregon’s Infrastructure Finance Authority (IFA), to complete the reservoir project. The original loan commitment from the IFA was \$232,100 with a principal forgiveness provision of \$154,260. After initial financing approval from the Commission, IFA increased its overall loan commitment to \$364,000 due to additional necessary costs required to finish the project. IFA also provided complete forgiveness of the loan thus eliminating any future loan repayment requirements.

Harbor Water has begun its operational test of Pelican Bay’s system. Term 1 of the annexation agreement includes a provision that the new reservoirs must be operational for

¹ See *In re Cline Butte Water, LLC*, OPUC Docket No. UP 345, Order No. 17-156 at 3-4 (May 1, 2017) (“[W]e apply a ‘no harm’ standard in approving water utility transfer applications”).

three months prior to annexation. The term is discussed below in the scope and terms of the annexation agreement.

Upon finalization of the annexation, Pelican Bay will not be rate or service regulated by the Commission, will dissolve as an entity, and the system will proceed to operate under the jurisdiction of Harbor Water.

As part of its investigation, Staff issued eight information requests related to the terms of the annexation and anticipated impacts to customers. Staff also investigated Harbor Water's financial and operational ability to assume the addition of customers from Pelican Bay.

Scope and Terms of the Annexation Agreement

The sales price of the property is \$0, and the Application states that the net book value of the water system is \$389,165. All property owned by the Company is included in this transaction. This includes water lines, pumping equipment, reservoirs, telemetry, and other assets. As a requirement of the Annexation Agreement (Agreement) between Pelican Bay and Harbor Water, the new reservoirs will be operational for a period of three months and will have been inspected and approved by an engineer. Staff reviewed the Agreement and noted no unusual or restrictive terms to the agreement.

Public Interest Compliance

Discussions over a possible merger with Harbor Water have been taking place since Pelican Bay's previous rate case (UW 143) in 2010. The Company has also had frequent communications with all current customers over the last three years, and all residents have been very supportive of the annexation.

Consolidation with Harbor Water will help ensure services to residents in the Pelican Bay Heights area are continued into the future. The current Pelican Bay customers will see multiple benefits from the annexation to Harbor Water. The reservoir tanks are gravity fed and provide increased water pressure, water quality standards, and promote water system efficiencies. Fire hydrants will be fully operational and provide the necessary pressure for proper fire suppression.² Former Pelican Bay customer rates may be lower under Harbor Water as Staff's analysis found that Harbor Water customer rates are currently more than 50 percent less than Pelican Bay residents pay, however, Staff notes that Term 4 of the

² See in *Pelican Bay Heights Water System LLC*, OPUC Docket UF 4295, Order No. 15-403 (December 15, 2015) Appendix A page 3 of 4 ("Consolidation with Harbor Water will help ensure services to residents in the Pelican Bay Heights area are continued into the future. The reservoir tanks will be gravity fed and provide increased water pressure, water quality standards, and promote water system efficiencies. Fire hydrants will become fully operational and provide the necessary pressure for fire suppression. Based on customer letters, emails, as well as oral communications with Pelican Bay, most residents appear supportive of the annexation").

Annexation Agreement allows Harbor Water to change the rate structure charged to residents of Pelican Bay.

As described above, the Agreement also provides for a test run of facilities to ensure that customers can continue to be served at the same or better service quality than they currently experience. If there are issues with the operation of the system, the Agreement will not close. This ensures that customers are provided adequate service by Harbor Water.

Harbor Water operates on a fiscal year ending June 30. Staff has reviewed Harbor Water's Annual Financial Reports for the years ended June 30, 2014 and June 30, 2015, the latest annual reports available.

Staff found that Harbor Water incurred an operating loss for each of those years. Harbor Water had an operating loss of \$94,680 for the year ended June 30, 2014 and an operating loss of \$143,268 for the year ended June 30, 2015. As a mitigating factor, Harbor Water had unrestricted reserves, which may be used to meet the district's obligations, of over \$2.9 million on its balance sheet at the end of both of the financial periods reviewed by Staff. Operating expense during those years ranged from \$753,796 to \$801,485. Harbor Water has more than three years of operating expense in its unrestricted reserves.

As a further mitigating factor regarding Harbor Water's operating loss, Harbor Water's Board of Directors can raise Harbor Water's rates, if necessary.

Staff also reviewed Harbor Water's draft Annual Financial Report for 2016, which has not been finalized.

Based on its review, Staff believes Harbor Water has the financial ability to operate after the annexation.

Conclusion

Staff concludes that the annexation of Pelican Bay to Harbor Water meets the public interest, no harm standard, and should be approved subject to Staff's conditions.

PROPOSED COMMISSION MOTION:

Approve the annexation of Pelican Bay to Harbor Water, subject to the conditions stated in Staff's recommendations in this memorandum.