

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA



**FILED**  
1-21-14  
04:59 PM

Application of California-American Water Company (U210W) for Approval of the Monterey Peninsula Water Supply Project and Authorization to Recover All Present and Future Costs in Rates.

Application 12-04-019  
(Filed April 23, 2012)

**OPENING BRIEF  
OF THE OFFICE OF RATEPAYER ADVOCATES**

**MARIA L. BONDONNO**  
Attorney

Office of Ratepayer Advocates  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102  
Tel: (415) 355-5594  
Fax: (415) 703-1673  
Email: maria.bondonno@cpuc.ca.gov

**RICHARD L. RAUSCHMEIER**  
Program and Project Supervisor

Office of Ratepayer Advocates  
Communications & Water Policy Branch  
California Public Utilities Commission  
505 Van Ness Avenue  
San Francisco, CA 94102  
Tel: (415) 703-2732  
Fax: (415) 703-1673  
Email: richard.rauschmeier@cpuc.ca.gov

January 21, 2014

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**I. INTRODUCTION**

Pursuant to Rule 13.11 of the California Public Utilities Commission’s Rules of Practice and Procedure and the Assigned Commissioner’s September 25, 2013 Amended Scoping Memo and Ruling, the Office of Ratepayer Advocates (“ORA”) hereby submits its Opening Brief on the Application of California-American Water Company (“Cal-Am”) for Approval of the Monterey Peninsula Water Supply Project (“MPWSP”).

On July 31, 2013, ORA joined Cal-Am and other parties to the proceeding in a motion for approval of two settlements: a comprehensive Settlement Agreement regarding the MPWSP and a specific Settlement Agreement regarding plant size. Because the two Settlement Agreements represent a reasonable and balanced resolution of the issues in the proceeding, ORA respectfully requests that the Commission adopt both settlements.

**II. THE SETTLEMENT AGREEMENTS PROVIDE A REASONABLE  
APPROACH TOWARD SOLVING MONTEREY’S LONG-TERM WATER  
CRISIS**

Monterey Peninsula residents and businesses have been struggling with water constraints since the 1940s.<sup>1</sup> Despite various attempts through the years to adequately address these constraints, the residents and businesses of Monterey continue to be subject to the danger of not possessing an adequate and reliable long-term water supply. The MPWSP, as presented in the two Settlement Agreements before the Commission, is reasonable and offers the clearest and

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<sup>1</sup> D.10-12-016, page 9.

most widely-supported approach towards solving Monterey’s long-term water crisis. As such, ORA recommends that the Commission adopt the two Settlement Agreements.

### **III. THE SETTLEMENT AGREEMENTS FAIRLY REPRESENT RATEPAYER INTERESTS**

In order to ensure that ratemaking related to the MPWSP would fairly represent the interests of ratepayers, ORA carefully reflected upon the guidance established by the Commission in the earlier Coastal Water Project proceeding.<sup>2</sup> Save for the increased urgency of finding a new source of water brought on by the current drought, little has changed in the three years since the Commission authorized construction of a desalination plant designed to produce 10 million gallons per day (“MGD”) at a cost of \$297.5 million with delivery pipelines costing \$106.9 million.<sup>3</sup> One thing that has changed, however, is the deadline requiring Cal-Am to terminate diversions from the Carmel River is now three years closer to the commencement of construction on any project.<sup>4</sup>

Through collaboration and extensive negotiation amongst the various parties in the instant proceeding, two Settlement Agreements have been entered into that, if authorized by the Commission, would allow Cal-Am to construct a 9.6 MGD plant at an expected cost of \$253.3 million with delivery pipelines expected to cost \$85.0 million.<sup>5</sup> Although these amounts are not absolute cost caps, the additional reporting requirements and Commission scrutiny that would be triggered if Cal-Am exceeded these caps do “provide incentive for cost control” and signal the “most probable cost” for the facilities.<sup>6</sup> More importantly, since these cost estimates are for “budgeting purposes” only,<sup>7</sup> nothing in the Settlement Agreements precludes the Commission from disallowing unreasonable or imprudent costs from entering rates as part of the Commission’s prudence review process.

Beyond establishing reasonable cost estimates and incentives for cost control, ORA’s decision to sign the Settlement Agreements is designed to ensure that customers do not have to

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<sup>2</sup> Application (A.04-09-019) of Cal-Am for a Certificate of Public Convenience and Necessity to Construct and Operate its Coastal Water Project.

<sup>3</sup> D.10-12-016, Findings of Fact #45, #106, and #194.

<sup>4</sup> *Id.*, Conclusion of Law #18.

<sup>5</sup> Settlement Agreement (“SA”), Sections 6.7 and 7.2.

<sup>6</sup> Reporter’s Transcript (RT), page 2206, lines 4-12.

<sup>7</sup> SA, Sections 6.6.

compensate a utility for returns on investment until a project is demonstrated to be used and useful. Only after the “desalination facilities go into service” and the conveyance pipelines are actually “used and useful” will project costs be included in utility plant in service and ratebase.<sup>8</sup> No facilities or project components will be deemed “used and useful” for ratemaking purposes until they actually are found to be used and useful in providing utility service.

#### **IV. EXTRAORDINARY CIRCUMSTANCES OCCASIONALLY JUSTIFY EXTRAORDINARY RATEMAKING**

With a most probable capital cost to be borne by the customers of the Monterey District that is nearly twice the last authorized revenue requirement of all of Cal-Am’s water districts combined,<sup>9</sup> the MPWSP being presented to the Commission can easily be considered extraordinary. In order to protect ratepayers and mitigate the cost of compounding interest and the rate impacts that would follow a extraordinarily large capital addition under traditional ratemaking, ORA has included provisions in the comprehensive Settlement Agreement that will permit customer contributions (Surcharge #2) to be collected and applied towards lowering the final project ratebase on which Cal-Am is authorized to earn an investment return.<sup>10</sup>

ORA points out, however, that this type of non-traditional ratemaking to lower ratebase must be balanced against the risk of customers contributing to a project that unexpectedly becomes unviable. The comprehensive Settlement Agreement achieves this balance by having safeguards, such as placing restrictions upon the timing and use of customer contributions. For example, Section 12.1(c) of the comprehensive Settlement Agreement, Surcharge #2 would begin only after collection of previously authorized customer surcharges (Surcharge #1) end. By delaying the start of Surcharge #2, the ratepayers of Monterey receive greater assurance that the funds collected under Surcharge #2 will actually contribute to a viable project since project viability is likely to increase with further project development.

Additionally, Section 12.2(a) of the comprehensive Settlement Agreement requires the initial \$35 million of customer contributions to be applied to the tangible and more routine

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<sup>8</sup> SA, Sections 6.8(c) and 7.3(c).

<sup>9</sup> Attachment 2 of Cal-Am’s Compliance Filing (11/19/13) presents the most probable total project cost (Settlement Tier 2 Advice Letter Cap) as \$347.8 million (desalination facilities of \$253.3 plus pipeline facilities of \$85.5). Page 2 of Commission Decision D.12-06-016 adopted 2012 revenue requirements totaling \$185.6 for Cal-Am’s districts.

<sup>10</sup> SA, Section 12.

construction of conveyance pipelines, which might prove useful even if a different supply project is ultimately built. Section 12.2 of the comprehensive Settlement Agreement includes a final safeguard against customers contributing to an unviable or abandoned project, by permitting the remaining balance of Surcharge #2 funds to be applied to desalination plant costs only after permits required to commence construction have been obtained.

## V. CONCLUSION

There is an undisputed need to find an alternative to the water supply that Cal-Am draws from the Carmel River. With the Settlement Agreements that are before the Commission, an opportunity exists to move forward with a project that has the widest and most popular support of any alternative ever presented to the Commission. After decades of contentious discussions and hardened perspectives regarding water supplies on the Monterey Peninsula, it is unlikely that any project could ever achieve the unanimous support and the utopian designation of a perfect project. However, contained within the Settlement Agreements, is a good project that balances the multiple and varied interests of the parties.

In regard to ORA and the ratepayers that ORA represents, the Settlement Agreements achieve a project framework that is far more beneficial than any other project the Commission has considered and authorized. Ratepayer protections such as reasonable estimates of the most probable project costs, limitations placed upon the use of customer contributions, and the assurances of Cal-Am to “striv[e] to get the lowest cost financing at all times to finance the project,”<sup>11</sup> combine to make for a balanced settlement. Hence, ORA respectfully requests that the Commission adopt both Settlement Agreements and pave the way to solving Monterey’s long-term water problem.

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<sup>11</sup> RT (Stephenson) page 2220, lines 13-15; and SA, Section 11.6(b).

Respectfully submitted,

/s/ MARIA L. BONDONNO

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MARIA L. BONDONNO

Attorney for the Office of Ratepayer Advocates

California Public Utilities Commission

505 Van Ness Ave.

San Francisco, CA 94102

Tel: (415) 355-5594

Fax: (415) 703-1673

Email: [maria.bondonno@cpuc.ca.gov](mailto:maria.bondonno@cpuc.ca.gov)

January 21, 2014