

**BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA**



**FILED**

07-11-12  
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.

A.12-04-019  
(Filed April 23, 2012)

**CALIFORNIA-AMERICAN WATER COMPANY OPENING BRIEF  
ON LEGAL ISSUES FOR EARLY RESOLUTION**

Lori Anne Dolqueist  
Jack Stoddard  
Manatt, Phelps & Phillips  
One Embarcadero Center, 30th Floor  
San Francisco, CA 94111  
(415) 291-7400  
ldolqueist@manatt.com

Attorneys for Applicant  
California-American Water Company

Sarah E. Leeper  
California-American Water Company  
333 Hayes Street  
Suite 202  
San Francisco, CA 94102  
(415) 863-2960  
sarah.leeper@amwater.com

Attorney for Applicant  
California-American Water Company

July 11, 2012

## TABLE OF CONTENTS

	Page
I. INTRODUCTION .....	1
II. THE MONTEREY COUNTY ORDINANCE ENCROACHES ON THE COMMISSION’S JURISDICTION OVER WATER UTILITY FACILITIES .....	1
A. The Monterey County Ordinance Is Expressly Preempted by the California Constitution.....	2
B. The California Public Utilities Code Fully Occupies the Field of Regulating Water Utilities. ....	4
C. Municipal Law Is Preempted Where It Conflicts with the Commission’s Authority Over Public Utilities.....	6
III. THE MONTEREY COUNTY ORDINANCE ALSO EXCEEDS THE COUNTY’S JURISDICTION, CONFLICTS WITH STATE POLICY, AND IS VAGUE AND AMBIGUOUS.....	8
A. The Monterey County Ordinance Exceeds the County’s Delegated Authority .....	8
B. The Monterey County Ordinance Conflicts with State Policy Regarding Desalination .....	9
C. The Monterey County Ordinance is Vague and Ambiguous.....	9
IV. THE WATER RIGHTS CLAIMS REGARDING SALINAS VALLEY GROUNDWATER BASIN WATER DO NOT AFFECT THE FEASIBILITY OF THE PROJECT.....	10
A. Project Configuration.....	12
B. California American Water Intends to Return All Groundwater Developed from the SVGB, and, Therefore, Does Not Intend to Initiate an Appropriation of Such Water for Beneficial Use .....	14
C. To the Extent Water Rights are Required for the Monterey Peninsula Water Supply Project, California American Water May Lawfully Initiate and Develop An Appropriative Groundwater Right in the Circumstances of the Proposed Project .....	15
D. The Annexation Agreement Does Not Affect the Project or Restrict California American Water’s Actions .....	16
E. The Monterey Peninsula Water Supply Project is in Furtherance of Prevailing State Water Policies and Laws .....	17
F. The Monterey Peninsula Water Supply Project is Consistent With the Agency Act .....	18
V. THE OUTFALL AGREEMENT DOES NOT PREVENT CALIFORNIA AMERICAN WATER FROM UTILIZING MRWPCA’S OUTFALL CAPACITY.....	19
A. Performance of the Outfall Agreement Will Likely Be Excused .....	20
1. The Implied Condition of the Outfall Agreement is Not Satisfied.....	20
2. Performance of the Outfall Agreement is Impossible.....	21

**TABLE OF CONTENTS**  
(continued)

	<b>Page</b>
3. The Purpose of the Outfall Agreement has Been Frustrated .....	22
VI. THE GROUNDWATER REPLENISHMENT PROJECT WATER RIGHTS ISSUES ARE DIFFERENT BECAUSE CALIFORNIA AMERICAN WATER IS SIMPLY SEEKING TO PURCHASE WATER .....	23
VII. CONCLUSION.....	24

## TABLE OF AUTHORITIES

Page

### STATE CONSTITUTION

Cal. Const., Article X, § 2.....	17, 18
Cal. Const., Article XI, § 1 .....	4
Cal. Const., Article XI, § 6 .....	4
Cal. Const., Article XI, § 7 .....	2
Cal. Const., Article XII, § 8.....	2, 4, 7

### STATE STATUTES

23 Cal. Code Regs. § 663.....	13
Health & Saf. Code § 116270(g) .....	8
Health & Saf. Code § 116330(a).....	8
Pub. Util. Code § 451.....	2
Pub. Util. Code § 701.....	3, 4
Pub. Util. Code § 762.....	3
Pub. Util. Code § 768.....	3
Pub. Util. Code § 770.....	2
Pub. Util. Code § 1001.....	3
Wat. Code Appendix § 52-21 .....	18
Wat. Code § 1010 .....	18
Wat. Code § 1200 .....	11
Wat. Code § 1201 .....	11
Wat. Code § 12946 .....	9
Wat. Code § 12948 .....	9

### STATE CASES

<i>Burr v. Maclay Rancho Water Co.</i> (1908) 154 Cal. 428 .....	17
<i>Burr v. Maclay Rancho Water Co.</i> (1911) 160 Cal. 268 .....	15
<i>California Water &amp; Telephone Company v. County of Los Angeles</i> (1967) 253 Cal. App. 2d 16.....	2, 5, 6

**TABLE OF AUTHORITIES**  
(continued)

	<b>Page</b>
<i>City of Los Angeles v. Pomeroy</i> (1899) 124 Cal. 597 .....	11
<i>Consumers Lobby Against Monopolies v. Public Utilities Com.</i> (1979) 25 Cal.3d 891.....	3, 4
<i>Corona Foothill Lemon Company v. Lillibridge</i> (1937) 8 Cal.2d 522 .....	17
<i>Federal Leasing Consultants, Inc. v. Lipsett Company, Inc.</i> (1978) 85 Cal.App.3d Supp. 44.....	22
<i>H. Hackfeld &amp; Co., Ltd. v. Castle</i> (1921) 186 Cal. 53 .....	20, 22
<i>Habitat Trust for Wildlife, Inc. v. City</i> (2009) 175 Cal.App.4th 1306.....	20, 21, 22
<i>Harbor Carriers, Inc. v. City of Sausalito</i> (1975) 46 Cal.App.3d 773 .....	5, 6, 7
<i>Hartwell v. Superior Court</i> (2002) 27 Cal.4th 256.....	8
<i>Johnson v. Atkins</i> (1942) 53 Cal.App.2d 430 .....	23
<i>Katz v. Walkinshaw</i> (1903) 141 Cal. 116.....	15
<i>La Cumbre Golf and Country Club v. Santa Barbara Hotel Co.</i> (1928) 205 Cal. 422 .....	20
<i>Los Angeles Ry. Corp. v. Los Angeles</i> (1940) 16 Cal. 2d 779 .....	5
<i>Los Angeles v. San Fernando, et al.</i> (1975) 14 Cal.3d 199 .....	16
<i>Orange County Air Pollution Control Dist. v. Public Util. Com.</i> (1971) 4 Cal.3d 945 .....	5
<i>Pasadena v. Alhambra</i> (1949) 33 Cal.2d 908.....	14, 15, 16, 17
<i>Peabody v. Vallejo</i> (1935) 2 Cal.2d 351 .....	15, 17
<i>Pomona Land &amp; Water Co. v. San Antonio Water Co.</i> (1908) 152 Cal. 618 .....	18
<i>Public Utilities Com. v. Energy Resources Conservation &amp; Dev. Com.</i> (Cal. App. 1st Dist. 1984).....	5
<i>Simons v. Inyo Cerro Gordo Min. &amp; Power Co.</i> (1920) 48 Cal.App.524 .....	14
<i>Southern California Gas Co. v. City of Vernon</i> (1995) 41 Cal. App.4th 209.....	3, 6

**OTHER AUTHORITIES**

Monterey County Code of Ordinances, Title 10, Chap. 10.72 .....	1, 2, 4, 10
Slater, California Water Law and Policy (Vol. 1, 1995) .....	17
SWRCB Decision No. D-379 .....	14

**BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF CALIFORNIA**

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.

A.12-04-019  
(Filed April 23, 2012)

**CALIFORNIA-AMERICAN WATER COMPANY OPENING BRIEF  
ON LEGAL ISSUES FOR EARLY RESOLUTION**

**I. INTRODUCTION**

Pursuant to Rule 13.1 of the Rules of Practice and Procedure of the California Public Utilities Commission (“Commission”) and as directed by Administrative Law Judge (“ALJ”) Weatherford in his ruling on June 1, 2012, California-American Water Company (“California American Water”) hereby submits its opening brief on the two issues identified in the June 1 ruling: (1) whether an ordinance limiting the ownership and operation of a desalination facility in Monterey County to public agencies is preempted by Commission authority and (2) whether the Monterey Peninsula Water Supply Project is feasible in light of the water right claims of various entities. As California American Water discusses in more detail below, the Monterey County Ordinance is invalid with respect to California American Water and the water rights claims do not affect the feasibility of the Monterey Peninsula Water Supply Project.

**II. THE MONTEREY COUNTY ORDINANCE ENCROACHES ON THE COMMISSION’S JURISDICTION OVER WATER UTILITY FACILITIES**

Monterey County Code Chapter 10.72 (“the Monterey County Ordinance”) requires an applicant for a desalination facility to obtain permits from the Monterey County Director of Environmental Health in order to construct and operate a desalination facility, and

provide “assurances that each facility will be owned and operated by a public entity.”<sup>1</sup> Under the Monterey County Ordinance, applicants must also provide a technical report that includes detailed plans and specifications, water quality information, physical descriptions of the proposed system, and financial assurance information.

Local legislation in conflict with general law is void under the California Constitution.<sup>2</sup> A local ordinance conflicts with general law if the ordinance duplicates, contradicts, or enters an area fully occupied by general law, either expressly or by legislative implication.<sup>3</sup> If the subject matter or field of the legislation has been fully occupied by the State, there is no room for supplementary or complementary local legislation, even if the subject is otherwise an appropriate area of local concern.<sup>4</sup> If local legislation conflicts with general law or is a matter of statewide rather than strictly local concern, the local ordinance is void, whether or not the general law completely occupies the field, however defined.<sup>5</sup>

The Monterey County Ordinance is invalid vis-à-vis the Commission’s jurisdiction because it is expressly preempted by the California Constitution, it attempts to regulate public utilities in an area where the Commission’s regulation fully occupies the field, and it conflicts with the authority given to the Commission by the Legislature in the Public Utilities Code to ensure utilities provide adequate service.

**A. The Monterey County Ordinance Is Expressly Preempted by the California Constitution**

Article XII, Section 8 of the California Constitution states that a city, county, or other public body may not regulate matters over which the Legislature grants regulatory power to the Commission. Sections 451 and 770 of the Public Utilities Code specify the Commission’s authority to require adequate service by regulated utilities. The Commission is empowered to do

---

<sup>1</sup> Monterey County Code of Ordinances, Title 10, Chap. 10.72, available at <<http://library.municode.com/index.aspx?clientId=16111>>

<sup>2</sup> Cal. Const., art. XI, § 7 (“A county or city may make and enforce within its limits all local, police, sanitary and other ordinances and regulations not in conflict with general laws.”)

<sup>3</sup> *California Water & Telephone Company v. County of Los Angeles* (1967) 253 Cal. App. 2d 16, 18.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

“all things ... necessary and convenient in the exercise of such power and jurisdiction.”<sup>6</sup> In addition, the Commission is authorized and obligated to regulate all aspects of utility facilities and infrastructure: no water utility may construct any major water facility without first obtaining a certificate of public convenience and necessity (“CPCN”) from the Commission;<sup>7</sup> the Commission must fix the rules, practices, equipment, appliances, facilities, service or methods to be observed, furnished, constructed enforced or employed; the Commission must order extensions of existing facilities or extension of new facilities where the Commission finds it will promote the security and convenience of the public or ensure adequate service;<sup>8</sup> and the Commission may establish rules and regulations to require public utilities to construct and maintain its plant, system and facilities so as to promote the health and safety of the utility’s customers, employees and the public.<sup>9</sup> Thus, the Legislature has clearly granted regulatory power to the Commission regarding the adequacy of service by public utilities and the composition of the facilities used to provide such service.

The courts have interpreted this section broadly. In *Southern California Gas Co. v. City of Vernon* (1995) 41 Cal. App.4th 209, a gas utility challenged the city’s denial of an encroachment permit to install pipelines under city streets. The court affirmed judgment for the gas utility, holding that the City could not regulate matters over which the Commission is accorded exclusive regulatory power under the state constitution and that the utility was entitled to issuance of a permit as a matter of law.

To the extent that the Monterey County Ordinance seeks to regulate the “plans and specifications, water quality information, and physical descriptions of the proposed system,” the County is seeking to regulate “the equipment, appliances, facilities, service or methods to be observed, furnished, constructed enforced or employed” over which the Commission has regulatory power under the Public Utilities Code. Moreover, to the extent that the Monterey

---

<sup>6</sup> Pub. Util. Code § 701; and see *Consumers Lobby Against Monopolies v. Public Utilities Com.* (1979) 25 Cal.3d 891, 905 [the Commission’s powers are liberally construed].

<sup>7</sup> Pub. Util. Code § 1001.

<sup>8</sup> Pub. Util. Code § 762.

<sup>9</sup> Pub. Util. Code § 768.

County Ordinance seeks to require “financial assurances” related to the operation of a desalination facility, as applied to a public utility, the Monterey County Ordinance seeks to regulate the financial health of a public utility, which is clearly the sole authority of this Commission. The Public Utilities Code empowers the Commission to regulate water utilities “by fixing rates and establishing rules for all public utilities within its jurisdiction.”<sup>10</sup> In addition, the Commission is empowered to do “all things ... necessary and convenient in the exercise of such power and jurisdiction.”<sup>11</sup> Thus, the Monterey County Ordinance is expressly preempted by Article XII, Section 8 of the California Constitution because it attempts to regulate matters over which the Legislature has granted regulatory power to the Commission.

California American Water notes that it is not alone in its conclusion that the ordinance is preempted. The Commission’s General Counsel has likewise warned that “to the extent this ordinance purports to limit sponsorship of a desalination project only to governmentally-owned enterprises, and more particularly to prohibit such sponsorship by a private, for-profit, investor-owned utility company regulated by our Commission – such as CalAm – *the ordinance would be preempted and of no legal validity under settled principles of California law.*”<sup>12</sup> In addition, Monterey County’s own County Counsel advised, “it appears that if the PUC issues a CPCN authorizing the Project, the County will not have the power to deny the Project when it considers an application for land use authorization.”<sup>13</sup>

**B. The California Public Utilities Code Fully Occupies the Field of Regulating Water Utilities.**

The Monterey County Ordinance is preempted, not only because it is expressly unconstitutional under Article XII, Section 8 of the California Constitution, but also because the

---

<sup>10</sup> Cal. Const., art. XI, §§ 1,6.

<sup>11</sup> Pub. Util. Code § 701; and see *Consumers Lobby Against Monopolies v. Public Utilities Com.* (1979) 25 Cal.3d 891, 905 [the Commission’s powers are liberally construed].

<sup>12</sup> Letter from Frank R. Lindh, Commission General Counsel, to Charles J. McKee, County of Monterey County Counsel, “Re: Monterey County Ordinance 10.72.030(B)”, dated April 18, 2012 (emphasis added).

<sup>13</sup> Memorandum to the County of Monterey Board of Supervisors from David Nawi, Acting County Counsel, “Re: Proposed Desalination Facility of Moss Landing”, dated April 1, 2003. This memorandum was previously attached to *California-American Water Company Reply to Protests* filed on June 4, 2012 and is now included in the *Direct Testimony of Richard C. Svindland*, dated April 23, 2012 (“Svindland Direct”), Attachment 7.

State has fully occupied the field of regulation of privately owned water utilities.

Relying on the breadth of the Public Utilities Code, courts have consistently held that local or municipal regulation of public utilities is impliedly preempted by the Commission's jurisdiction. The Commission has "paramount jurisdiction in cases where it has exercised its authority, and its authority is pitted against that of a local government involving a matter of statewide concern."<sup>14</sup> In other words, there is no room for local regulation of public utilities.

In *California Water & Telephone Co. v. County of Los Angeles* (1967) 253 Cal.App.2d 16 ("*California Water & Telephone*"), the court struck down as unconstitutional a county ordinance that required any person that supplied domestic water to more than one customer to obtain a permit as a condition precedent to the construction of any portion of the water system.<sup>15</sup> The purported purpose of the ordinance was to promote fire safety, an area otherwise within a municipality's authority over health and safety. Nevertheless, the court found that "the construction, design, operation and maintenance of public water utilities is a matter of state-wide concern."<sup>16</sup> The court reasoned that the control of design and construction of water utility facilities "is not a municipal affair subject to a checkerboard of regulations by local governments" and is within the exclusive statewide jurisdiction of the Commission.

Similarly, in *Los Angeles Ry. Corp. v. Los Angeles* (1940) 16 Cal. 2d 779, a City of Los Angeles ordinance was found unconstitutional on the grounds that the ordinance, which required crews of at least two persons on all streetcars in the city, conflicted with a Railroad Commission order authorizing operation of streetcars by one person.

The Monterey County Ordinance is analogous to the Los Angeles County ordinance struck down in *California Water & Telephone*. As in *California Water & Telephone*, the Monterey County Ordinance is enrolled as a health and safety regulation. As the court noted in that case, however, while the regulation of health and safety is otherwise a legitimate area of

---

<sup>14</sup>; *Public Utilities Com. v. Energy Resources Conservation & Dev. Com.* (Cal. App. 1st Dist. 1984) 150 Cal. App. 3d 437, 451-452; *Harbor Carriers, Inc. v. City of Sausalito* (1975) 46 Cal.App.3d 773, 775; *Orange County Air Pollution Control Dist. v. Public Util. Com.* (1971) 4 Cal.3d 945, 953 at fn. 7.

<sup>15</sup> *California Water & Telephone Co. v. County of Los Angeles* (1967) 253 Cal.App.2d 16, 21.

<sup>16</sup> *Id.* at 30.

municipal concern, it is invalid if it encroaches on the Commission's jurisdiction. As explained above, the Monterey County Ordinance concerning the construction, operation and ownership of desalination facilities both encroaches on and conflicts with the Commission's jurisdiction over water utility facilities and infrastructure. The required technical report, which includes detailed plans and specifications, water quality information, a physical description of the proposed system, and financial assurance information, covers the same ground as the Commission's CPCN process. It is not relevant that the purpose of the ordinance may be to promote health and safety if the subject of the regulation is substantially the same as the subject of the Commission's CPCN process and general regulatory oversight. Thus, just as the Los Angeles County ordinance was invalid, so too is the Monterey County Ordinance.

Clearly, the Commission's broad authority over water utility facilities leaves no room for additional and conflicting municipal regulation. As the court in *California Water & Telephone* stated "[n]o profound exegesis of the Water Ordinance... the Public Utilities Code, and the [C]ommission's regulations promulgated pursuant thereto is necessary to conclude that the Water Ordinance as applied to [the public utility] conflicts with general law."<sup>17</sup>

Moreover, the Monterey County Ordinance is in conflict with state law regarding investor owned public utilities because it reserves to Monterey County the power to decide what types of entities can own and operate desalination facilities within the County. If this type of local ordinance were allowed to stand, then any county could prohibit private ownership and operation of all types of utility facilities, thereby undermining the state's authority to provide statewide uniformity of regulation over utility facility operations.<sup>18</sup>

**C. Municipal Law Is Preempted Where It Conflicts with the Commission's Authority Over Public Utilities**

Even where local legislation is otherwise valid, it is void if it interferes with the Commission's jurisdiction. In *Harbor Carriers v. City of Sausalito* (1975) 46 Cal.App.3d 773,

---

<sup>17</sup> *California Water & Telephone Co. v. County of Los Angeles*, supra, 253 Cal.App.2d 16 at 26.

<sup>18</sup> *Southern Cal. Gas Co. v. City of Vernon* (1995) 41 Cal. App. 4th 209, 217 ("goal of statewide uniformity... would be defeated if a municipality ... could enlarge upon the standards promulgated by the PUC").

775, (“*Harbor Carriers*”) the court found a city zoning ordinance preempted by a Commission CPCN as it applied to the location of a harbor ferry terminal and docking facility. The court held that “to the extent that the city’s zoning ordinance is applied to prevent establishment of any terminal in Sausalito, it must give way to the [Commission’s] grant of the right to operate a service to and from Sausalito.”<sup>19</sup> The court further concluded that a city terminal site was necessarily contemplated by the Commission’s CPCN and ordered the city to afford the opportunity for a reasonable terminal site.

The Monterey Peninsula Water Supply Project is a major water facility. California American Water is subject to the jurisdiction of the Commission and, therefore, must obtain a CPCN before proceeding with construction of the desalination facility and its appurtenances. If the Commission were to determine that the Monterey Peninsula Water Supply Project is a reasonable and prudent means of providing adequate water service to California American Water’s Monterey customers and in the public interest, then the Monterey County Ordinance would conflict with the Commission’s order, as was the case with to the City of Sausalito’s zoning ordinance. If the Commission’s approval did not preempt the Monterey County Ordinance, it could prevent California American Water from developing a project deemed to be reasonable and prudent by the Commission, and thus preclude California American Water from providing adequate service to its customers. Accordingly, the Monterey County Ordinance must yield to the Commission’s jurisdiction.

Because the Monterey County Ordinance: is expressly preempted by Article XII, Section 8 of the California Constitution; encroaches on the Commission’s statewide jurisdiction over water utility facilities; and would conflict with state law should this Commission authorize the Monterey Peninsula Water Supply Project, the Monterey County Ordinance cannot be lawfully applied to California American Water’s proposed desalination plant.

---

<sup>19</sup> *Harbor Carriers v. City of Sausalito* (1975) 46 Cal.App.3d 773, 775.

### **III. THE MONTEREY COUNTY ORDINANCE ALSO EXCEEDS THE COUNTY'S JURISDICTION, CONFLICTS WITH STATE POLICY, AND IS VAGUE AND AMBIGUOUS**

#### **A. The Monterey County Ordinance Exceeds the County's Delegated Authority**

The California Department of Public Health ("DPH," formerly the State Department of Health Services) is the agency designated to issue permits to operate public water systems that serve drinking water to more than 200 customers and to regulate the construction or additions to water supply for such systems. In this area, the DPH and the Commission have concurrent jurisdiction.<sup>20</sup> The California Safe Drinking Water Act provides:

It is the further intent of the Legislature to establish a drinking water regulatory program within the State Department of Health Services in order to provide for the orderly and efficient delivery of safe drinking water within the state and give the establishment of drinking water standards and public health goals greater emphasis and visibility within the state department.<sup>21</sup>

The California Safe Drinking Water Act provides for local administration and enforcement of Safe Drinking water laws and regulations only in certain limited instances. The Health & Safety Code clearly states, "...this delegation shall not include the regulation of community water systems serving 200 or more service connections."<sup>22</sup>

Although Monterey County has been delegated primacy for regulation of public water systems serving fewer than 200 customers,<sup>23</sup> California American Water serves approximately 40,000 customers in its main Monterey County District system, and the DPH has not delegated regulation of California American Water to Monterey County.

The Monterey County Ordinance appears to regulate the operation of a public water system regardless of the number of connections, and, therefore, is expressly preempted by Section 116330(a) of the Health & Safety Code. Additionally, to the extent that the Monterey County Ordinance purports to impose various regulatory obligations that are duplicative of the California Safe Water Drinking Act, this area of regulation is completely occupied by the DPH.

<sup>20</sup> See *Hartwell v. Superior Court* (2002) 27 Cal.4th 256, 271.

<sup>21</sup> Health & Saf. Code § 116270(g).

<sup>22</sup> *Id.*, § 116330(a).

<sup>23</sup> See [www.cdpha.ca.gov/certlic/drinkingwater/Pages/Smallwatersystems.aspx](http://www.cdpha.ca.gov/certlic/drinkingwater/Pages/Smallwatersystems.aspx)

The Monterey County Ordinance far exceeds the boundaries of the County’s authority if the County applies it to a public water system that serves more than 200 connections – such as California American Water’s system.

**B. The Monterey County Ordinance Conflicts with State Policy Regarding Desalination**

The requirement that all applicants for a permit to operate a desalination plant in Monterey County must provide assurances that each facility will be owned and operated by a public entity creates a direct conflict with the Cobey-Porter Saline Water Conversion Act (1965). The California Legislature recognized the importance of the conversion of saline water to drinking water nearly 50 years ago and expressly recognized that the private sector can and should be involved in desalination.<sup>24</sup>

Additionally, in 1991, the Legislature, seeking to further support desalination, added a requirement that the Department of Water Resources “shall provide assistance to persons or entities with State and local desalination facility permit applications seeking to construct desalination facilities for reducing the concentration of dissolved solids in brackish groundwater or seawater in the State.”<sup>25</sup> If the Legislature had intended to exclude the private sector from desalination it would have done so. Instead, private agencies and corporations are expressly included.

**C. The Monterey County Ordinance is Vague and Ambiguous**

The Monterey County Ordinance purports to regulate desalination treatment facilities, defined as “a facility which removes or reduces salts from water to a level that meets drinking water standards and/or irrigation purposes.” It also requires “any person, firm, water utility, association, corporation, organization, or partnership, or any city, county, district, or any department or agency of the State” to obtain a permit from the Director of Environmental Health of the County of Monterey before commencing construction or operation of any desalination

---

<sup>24</sup> Wat. Code §§ 12946, 12948.

<sup>25</sup> *Id.*, § 12948.1.

treatment facility.<sup>26</sup> Despite clear language that a water utility can commence construction or operation of a desalination treatment facility if that entity (be it water utility, corporation, or otherwise) obtains a permit, the procedure for obtaining an operation permit requires an applicant to “provide assurances that each facility will be owned and operated by a public entity.”<sup>27</sup> The Monterey County Ordinance is, therefore, internally inconsistent and contradictory.

#### **IV. THE WATER RIGHTS CLAIMS REGARDING SALINAS VALLEY GROUNDWATER BASIN WATER DO NOT AFFECT THE FEASIBILITY OF THE PROJECT**

The Division of Ratepayer Advocates, Marina Coast Water District (“MCWD”), WaterPlus, and LandWatch Monterey County all raised the issue of whether California American Water must obtain water rights to extract groundwater from the Salinas Valley Groundwater Basin (“SVGB”),<sup>28</sup> with MCWD and Water Plus arguing that the lack of such rights would doom the Monterey Peninsula Water Supply Project. The Monterey Peninsula Water Supply Project, however, likely does not require “water rights” because California American Water proposes to use ocean water as its source water supply and will return to the SVGB all water that originates therefrom. Moreover, even if water rights were required, such rights would be appropriative in nature and may be acquired, developed and perfected consistent with well-established principals of California water law. Additionally, despite allegations to the contrary, the water development for the Monterey Peninsula Water Supply Project is consistent with the Monterey County Water Resources Agency Act (“Agency Act”). Therefore, although multiple parties have raised water rights issues related to the Monterey Peninsula Water Supply Project,<sup>29</sup> none of the these claims affect the feasibility of the Project.

All or almost all of the water produced by the Monterey Peninsula Water Supply

---

<sup>26</sup> Monterey County Code §10.72.010.

<sup>27</sup> Id. 10.72.030B.

<sup>28</sup> *Protest of The Division of Ratepayer Advocates*, filed May 25, 2012 (“DRA Protest”), p. 5; *Protest of Landwatch Monterey County to the Application of California-American Water Company (U 210 W) for Approval of The Monterey Peninsula Water Supply Project and Authorization to Recover All Present and Future Costs In Rates*, filed May 25, 2012 (“LandWatch Protest”), pp. 4, 7; *Marina Coast Water District’s Protest of A.12-04-019*, filed May 25, 2012 (“MCWD Protest”), p. 4; *Protest By Water Plus*, filed May 24, 2012 (“Water Plus Protest”), p. 4.

<sup>29</sup> See e.g., Water Plus Protest; LandWatch Protest; DRA Protest; MCWD Protest.

Project will be water that originates in the Pacific Ocean. As a threshold matter, water rights are not required for development, treatment and use of water pumped from the ocean or beneath the sea floor. California surface water rights laws apply only to waters flowing or present in lakes, rivers and streams - including subterranean streams flowing in known and definite channels.<sup>30</sup> California's groundwater rights laws apply only to "percolating groundwater," which is generally defined as water found beneath the ground surface that is not flowing within a "subterranean stream."<sup>31</sup> Percolating groundwater is found in geologic formations known as "groundwater basins," which have been defined as "hydrologic units containing one large aquifer or several connected and interrelated aquifers."<sup>32</sup> The ocean and ocean waters lack the essential geologic and physical characteristics of surface water or percolating groundwater, as those terms have long been defined and interpreted in California. For this reason, it is not surprising that there is no precedent for applying California water rights laws to the development of ocean water.<sup>33</sup>

Most questions about the Monterey Peninsula Water Supply Project have focused on the small volume of Project water that might originate from the SVGB. These questions appear to focus on (1) whether the Monterey Peninsula Water Supply Project will export groundwater from the SVGB to the Monterey Peninsula, and therefore initiate an appropriation of groundwater, and (2) whether it is legal to do this if the SVGB is in "overdraft."<sup>34</sup> California American Water's commitment to return to the SVGB all of the SVGB groundwater developed by the Monterey Peninsula Water Supply Project is, in effect, a commitment not to appropriate groundwater from the SVGB. Under these circumstances, there is no "appropriation" or "export" of groundwater from the SVGB.<sup>35</sup> However, to the extent that a court or other authorized regulatory body might determine that the Monterey Peninsula Water Supply Project

---

<sup>30</sup> See Wat. Code §§ 1200, 1201.

<sup>31</sup> See, e.g., *City of Los Angeles v. Pomeroy* (1899) 124 Cal. 597.

<sup>32</sup> See Todd, *Groundwater Hydrology* (1980), p. 47.

<sup>33</sup> This is not to say that other permits and entitlements are not required for the development and desalination of seawater, and California American Water intends to comply with all applicable permit requirements and obtain all entitlements required for the Project.

<sup>34</sup> RT 60:8-10 (ALJ Weatherford); see also RT 18:16-28 (Nancy Isakson/Salinas Water Coalition), RT 59:22 – 60:2 (Mark Fogelman/MCWD).

<sup>35</sup> This commitment also ensures compliance with Section 21 of the Agency Act.

involves an “appropriation” of groundwater from the SVGB, such appropriation is entirely legal and valid under California water law, whether or not the SVGB is considered to be in “overdraft.”

There is no State, County, or other permit or entitlement requirement for development of groundwater in the proposed location of the Monterey Peninsula Water Supply Project.<sup>36</sup> In this area of Monterey County, a prospective water user need only obtain a well construction permit from the county to begin pumping water from beneath the ground surface. Therefore, the fundamental water right question at issue for the Monterey Peninsula Water Supply Project is not whether California American Water needs to establish a “water right,” but rather it is whether a third party or other SVGB pumper would have some legal basis to enjoin the development of the Monterey Peninsula Water Supply Project. Based on the available modeling and technical information that concludes there will be no significant effects from the proposed slant well operations,<sup>37</sup> there is no basis for a court or other authorized regulatory body to prohibit the incidental production of the small volume of SVGB groundwater that may be developed by the Monterey Peninsula Water Supply Project.

#### **A. Project Configuration**

As proposed, the Monterey Peninsula Water Supply Project will include a system of approximately eight subsurface “slant wells” to be constructed on the CEMEX property north of Marina, between the Pacific Ocean (Monterey Bay) and Highway 1. Water pumped by the slant wells will be conveyed by pipe to a desalination plant to be constructed on vacant and disturbed land adjacent to the Monterey Regional Water Pollution Control Agency’s (“MRWPCA”) Regional Treatment Plant (“RTP”). Water produced at the desalination plant will be delivered directly to the Monterey Peninsula for municipal uses within the California American Water service area, or will be delivered to the Seaside Basin for aquifer storage,

---

<sup>36</sup> Unlike surface water rights, there is no established State, County or local application or permitting requirement for initiating or developing a “groundwater right”; rather, in most unadjudicated groundwater basins such as the SVGB, a groundwater right is established by pumping and beneficially using groundwater from the groundwater basin.

<sup>37</sup> Svindland Direct, Attachment 3.

recovery and subsequent municipal use in the California American Water service area.<sup>38</sup>

An amount of treated water, equal to the volume of Monterey Peninsula Water Supply Project water that is determined by testing to originate from the SVGB, will be delivered to an 80 acre-foot storage pond on the MRWPCA RTP property. This water will be blended with recycled wastewater produced by the MRWPCA at the RTP, and then distributed by the Monterey County Water Resources Agency (“MCWRA”) to the agricultural water users in the “Castroville Seawater Intrusion Project” (“CSIP”), which overlies the SVGB. The desalinated water from the Monterey Peninsula Water Supply Project, being of potable quality, is expected to significantly improve the quality of water deliveries to the CSIP. The water delivered to the MRWPCA and MCWRA also will contribute to the supply of agricultural water in the SVGB, in lieu of a like volume of groundwater pumped by overlying users, and thus will assist the MCWRA in its efforts to address seawater intrusion in the SVGB.

The Monterey Peninsula Water Supply Project slant wells will be configured at an angle to extend out from the shoreline and will draw seawater from beneath the seafloor. The wells will be constructed using modified vertical well construction methods to allow the wells to extract water with higher salinity than can be produced with conventional vertical wells. The angled drilling results in increased screen length, as compared to conventional vertical wells. Despite the use of slant wells, preliminary modeling results indicate that over the long term, the water pumped at the slant wells may include a small volume of seawater-contaminated groundwater originating from the SVGB.<sup>39</sup> Groundwater in this area of the SVGB currently is highly contaminated with seawater that has intruded many miles inland from the coast. This water generally is not suitable for beneficial uses without significant treatment and desalination.

---

<sup>38</sup> California American Water will utilize the Project water supply consistent with its authority to provide for drinking water and other municipal uses on the Monterey Peninsula. *See* 23 Cal. Code Regs. § 663 (defining “municipal use”).

<sup>39</sup> Existing modeling analyses assume full and successful implementation of MCWRA’s CSIP and Salinas Valley Water Project and uses future pumping predictions, and concludes that even under those conditions the volume of groundwater originating from the SVGB would be less than 3% of the total volume of water produced at the desalination plant.

**B. California American Water Intends to Return All Groundwater Developed from the SVGB, and, Therefore, Does Not Intend to Initiate an Appropriation of Such Water for Beneficial Use**

The taking of groundwater for other than overlying or riparian use in California is considered an “appropriative” use.<sup>40</sup> Under the California water rights law, a valid appropriation must include all the following elements: (1) the intent to apply the water to an existing or future beneficial use; (2) an actual diversion from the basin or natural channel; and (3) an application of the water within a reasonable time to some beneficial use.<sup>41</sup> It is not enough that an appropriator exercise dominion and control over pumped groundwater; the appropriator must intend to apply the water to a beneficial use, and must actually do so.

California American Water’s potential incidental development of groundwater from the SVGB does not satisfy the requisite elements required for an appropriation. As noted above, the slant wells are designed to pump seawater and to avoid or minimize the capture of groundwater from the SVGB; because the slant wells are located at the mouth of the SVGB, however, it is possible that they may capture water discharging from the basin in the transitional geology between the ocean and the basin. To address this possibility, the Project is designed such that any SVGB groundwater developed by the Project will be returned to the basin. This volume of “groundwater,” determined by ongoing monitoring, will be delivered to the MRWPCA and/or the MCWRA to be used by overlying groundwater users in the CSIP project. Under these circumstances, California American Water’s return of groundwater incidentally developed from the SVGB evidences California American Water’s intent not to apply the water to authorized municipal use within the California American Water service area. There is no “appropriation” of groundwater because all of the essential elements of an appropriation have not been satisfied.<sup>42</sup>

---

<sup>40</sup> See *Pasadena v. Alhambra* (1949) 33 Cal.2d 908, 925-926.

<sup>41</sup> Wells A. Hutchins, *The California Law of Water Rights* (“Hutchins”), at p. 108, citing *Simons v. Inyo Cerro Gordo Min. & Power Co.* (1920) 48 Cal.App.524, 537.

<sup>42</sup> See SWRCB Decision No. D-379 at p. 13 [finding: “Since an appropriation of water consists not only in taking the water under control but also subsequently applying it to beneficial use, the district is not authorized to appropriate water under the act but merely to take temporary possession thereof.”], available at <[http://www.waterboards.ca.gov/waterrights/board\\_decisions/adopted\\_orders/decisions/d0350\\_d0399/wrd379.pdf](http://www.waterboards.ca.gov/waterrights/board_decisions/adopted_orders/decisions/d0350_d0399/wrd379.pdf)>

**C. To the Extent Water Rights are Required for the Monterey Peninsula Water Supply Project, California American Water May Lawfully Initiate and Develop An Appropriative Groundwater Right in the Circumstances of the Proposed Project**

If, however, California American Water's pumping of SVGB groundwater were deemed by a court or other authorized regulatory body to be an "appropriation" of groundwater – despite California American Water's commitment to deliver all of that water to MRWPCA and MCWRA for use in the SVGB – the unique circumstances of the Monterey Peninsula Water Supply Project would still be found to be a valid exercise of appropriative groundwater rights. The slant well program in the similar North Marina project was extensively analyzed in the Commission's 2009 Final Environmental Impact Report ("FEIR"), and the Commission concluded that it would not adversely affect other groundwater users or groundwater elevations and conditions in the SVGB.<sup>43</sup> As a general rule, groundwater appropriations will not be enjoined unless the proposed appropriation can be shown to adversely affect other prior right holders in a groundwater basin.<sup>44</sup> Under the particular circumstances and conditions of the Monterey Peninsula Water Supply Project, there would be no reason for a court or regulatory body to enjoin or prohibit California American Water from incidentally appropriating a small volume of contaminated SVGB groundwater, particularly since that volume would be returned to the basin for beneficial use by overlying landowners.

Any SVGB groundwater that may be pumped by the Monterey Peninsula Water Supply Project is clearly surplus to the needs of all other SVGB water users because it can be pumped without adversely impacting other users or groundwater elevations and conditions in the SVGB. As the California Supreme Court has stated:

Public interest requires that there be the greatest number of beneficial uses that the supply can yield, and water may be

---

<sup>43</sup> A.04-09-019, Reference Exhibit B, *Final Environmental Impact Report*, dated October 30, 2009, Section 5.2.2.1.

<sup>44</sup> See, e.g., *Peabody v. Vallejo* (1935) 2 Cal.2d 351 at 374 ["[T]he appropriator may use the stream surface or underground or percolating water, so long as the land having the paramount right is not materially damaged"]; *Pasadena v. Alhambra* (1949) 33 Cal.2d at 930 ["[only] where . . . subsequent appropriators reduce the available supply and their acts, if continued, will render it impossible for the holder of a prior right to pump in the future, is there an enjoined invasion"]; *Burr v. Maclay Rancho Water Co.* (1911) 160 Cal. 268, 273 [discussing the doctrine established in *Katz v. Walkinshaw* (1903) 141 Cal. 116 and cases following it which provide that appropriative uses of groundwater can be enjoined only "if such taking is injurious to" prior right holders].

appropriated for beneficial uses subject to the rights of those who have a lawful priority. Any water not needed for the reasonable and beneficial uses of those having prior rights is excess or surplus water. In California, surplus water may rightfully be appropriated on privately owned land for non-overlying uses, such as devotion to a public use or exportation beyond the basin or watershed.<sup>45</sup>

Even if the SVGB were determined to be in “overdraft,”<sup>46</sup> therefore, the small volume of water that California American Water will pump from the SVGB is “surplus” or “supplemental safe yield” water, and subject to appropriation.<sup>47</sup>

**D. The Annexation Agreement Does Not Affect the Project or Restrict California American Water’s Actions**

MCWD argues that a 1996 *Annexation Agreement and Groundwater Mitigation Framework for Marina Area Lands* (“Annexation Agreement”), by and among MCWD, MCWRA, J.G. Armstrong Family Members, and RMC Lonestar, may limit California American Water’s proposed use of water for the Project. Among other applications, the Annexation Agreement applies to 400 acres of land along the Monterey Coast that includes the CEMEX Property where California American Water would develop the slant wells for the Monterey Peninsula Water Supply Project. The Agreement limits withdrawal of groundwater from the SVGB to 500 acre-feet per year of groundwater for use on the property, and prohibits export of SVGB groundwater from the basin.

There is no basis to interpret the Annexation Agreement as affecting the Monterey Peninsula Water Supply Project or otherwise restricting California American Water’s ability to appropriate a small amount of groundwater that may originate from the SVGB, particularly if that SVGB groundwater is returned to the SVGB as proposed. Whatever limitations and

---

<sup>45</sup> *Pasadena v. Alhambra* (1949) 33 Cal.2d 908, 925-926.

<sup>46</sup>It has been alleged by some parties to this proceeding that the SVGB is in “overdraft” and therefore appropriation from the SVGB is unlawful. Although there are areas of the SVGB where groundwater pumping has exceeded recharge rates, causing seawater intrusion and other indicia of groundwater level decline, there has not been any judicial determination of “overdraft.”

<sup>47</sup>Safe yield is defined as “the maximum average annual pumping which can be withdrawn annually from a groundwater supply under a given set of conditions without causing an undesired result.” *Los Angeles v. San Fernando, et al.* (1975) 14 Cal.3d 199, 278. To the extent the Project will pump seawater-contaminated groundwater from the SVGB without reducing the usable volume of groundwater in the basin, the Project will result in an increase of the maximum amount of pumping which can be withdrawn from the SVGB without causing an undesirable result, and thus supplements the safe yield of the SVGB.

restrictions the Annexation Agreement may have with respect to the use of groundwater on the CEMEX property, it has no application to the Monterey Peninsula Water Supply Project. Overlying or contractual groundwater rights, and associated uses and limitations, are legally distinct from appropriative groundwater rights and uses.<sup>48</sup> “Surplus water may rightfully be appropriated on privately owned land for nonoverlying purposes, such as devotion to a public use or exportation beyond the basin or watershed.”<sup>49</sup> “Unlike . . . overlying rights, [an] appropriative right is not dependent upon the ownership of real property. The right to use water under an appropriative right is distinct from the property through which the water flows or the land where the water is ultimately placed to beneficial use.”<sup>50</sup> Thus, assuming California American Water establishes an appropriative groundwater right in connection with the Monterey Peninsula Water Supply Project, that right would be legally distinct from the overlying or contractual groundwater rights (and any limitations thereon) that may be appurtenant to the use of groundwater on the CEMEX property.

**E. The Monterey Peninsula Water Supply Project is in Furtherance of Prevailing State Water Policies and Laws**

California American Water’s proposed development and desalination of otherwise unusable ocean water and groundwater, in a manner that does not adversely affect other SVGB groundwater users, and includes return of SVGB groundwater to the SVGB for beneficial use, significantly furthers the policy set forth in Article X, Section 2 of the California Constitution to foster the maximum beneficial use of water and to avoid waste.<sup>51</sup> The Monterey Peninsula Water Supply Project is also consistent with salvaged and developed water doctrines and statutes

---

<sup>48</sup> See *City of Pasadena v. City of Alhambra* (1949) 33 Cal.2d 908, 925 [“Appropriation” refers “to any taking of water other than riparian or overlying uses” (emphasis added)]; *Corona Foothill Lemon Company v. Lillibridge* (1937) 8 Cal.2d 522.

<sup>49</sup> *City of Pasadena v. City of Alhambra* (1949) 33 Cal.2d 908, 925-926.

<sup>50</sup> Slater, *California Water Law and Policy* (Vol. 1, 1995) § 2.16, at 2-98 [citing various cases].

<sup>51</sup> See, *Pasadena*, 33 Cal.2d at 926 [“It is the policy of the state to foster the beneficial use of water and discourage waste, and when there is a surplus, whether of surface or ground water, the holder of prior rights may not enjoin its appropriation”]; *Burr v. Maclay Rancho Water Co.* (1908) 154 Cal. 428, 436 [“It is not the policy of the law to permit any of the available waters of the country to remain unused, or to allow one having the natural advantage of a situation which gives him a legal right to water to prevent another from using it, while he, himself, does not desire to do so”]; *Peabody v. Vallejo* (1935) 2 Cal.2d 351, 370-371 [same].

encouraging the use of desalinated and reclaimed waters.<sup>52</sup>

**F. The Monterey Peninsula Water Supply Project is Consistent With the Agency Act**

In protests and prehearing conference statements, several parties alleged that the Monterey Peninsula Water Supply Project was inconsistent with the Agency Act.<sup>53</sup> Section 21 of the Agency Act provides:

The Legislature finds and determines that the Agency is developing a project which will establish a substantial balance between extraction and recharge within the Salinas River Groundwater Basin. For purposes of preserving that balance, no groundwater from that basin may be exported for any use outside the basin, except that use of water from the basin on any part of Fort Ord shall not be deemed such an export. If any export of water from the basin is attempted, the Agency may obtain from the superior court, and the court shall grant, injunctive relief prohibiting that exportation of groundwater.<sup>54</sup>

The Monterey Peninsula Water Supply Project is consistent with Section 21 of the Agency Act because California American Water proposes to deliver to the MRWPCA, for use in the SVGB, a volume of water equal to that groundwater that may incidentally be pumped by the Project. There will be no “export” of groundwater from the SVGB. Moreover, the export prohibition in Article 21 applies only to the extent that the proposed exportation negatively affects the balance of extraction and recharge in the SVGB. This reading of the Agency Act ensures that the statute is interpreted and implemented consistent with the requirements to maximize the beneficial use of water and avoid waste as set forth in Article X, Section 2 of the California Constitution, as discussed above. The proposed Monterey Peninsula Water Supply Project will not exacerbate (and actually will improve) the balance of extraction and recharge of usable groundwater.

---

<sup>52</sup> See *Pomona Land & Water Co. v. San Antonio Water Co.* (1908) 152 Cal. 618, 623-629 [holding that a water supply saved from loss or made available for use without injury to other water users may be used by the salvager]; see also, Wat. Code § 1010 [encouraging and facilitating use of desalinated and recycled water].

<sup>53</sup> LandWatch Protest, p. 7; MCWD Protest, pp. 4, 6; *Pre-Hearing Conference Statement of Landwatch Monterey County*, filed June 1, 2012, p. 5; *Marina Coast Water District's Prehearing Conference Statement*, filed June 4, 2012, pp. 7, 13, 16; *Prehearing Conference Statement of The County of Monterey and The Monterey County Water Resources Agency*, filed June 4, 2012, pp. 1-2.

<sup>54</sup> MWCWRA Act, Water Code Appendix § 52-21

**V. THE OUTFALL AGREEMENT DOES NOT PREVENT CALIFORNIA AMERICAN WATER FROM UTILIZING MRWPCA'S OUTFALL CAPACITY**

California American Water plans to use the MRWPCA excess outfall capacity for brine discharge with the desalination plant and has entered into preliminary discussions with MRWPCA staff with regard to negotiating and preparing a new agreement for required outfall capacity. MCWD and Water Plus claim that MCWD has a senior right to this outfall capacity, which could prevent California American Water's use of the MRWPCA outfall.<sup>55</sup> This claim is based on the February 2010 outfall agreement between MCWD and MRWPCA ("Outfall Agreement") permitting MCWD to use the MRWPCA's outfall based on the premise that MCWD would own and operate a desalination plant as part of the Regional Desalination Project ("RDP").<sup>56</sup>

The term of the Outfall Agreement is 34 years. On the face of the Outfall Agreement, it is clear that the purpose of the contract was to establish how MRWPCA's outfall would service the RDP Desalination Plant, which MRWPCA and MCWD assumed would be owned and operated by MCWD. As it now stands, the RDP will not be resurrected and MCWD will not own or operate the RDP Desalination Plant, although it is possible that MCWD will own and operate its own much smaller desalination plant.

As an initial matter, based on the technical analysis performed for California American Water, the outfall has sufficient capacity to accommodate MRWPCA average daily wastewater flows, the brine discharge from the Monterey Peninsula Water Supply Project desalination facility, and the original MCWD RDP brine discharge (even though the RDP will not be constructed).<sup>57</sup> Moreover, the purpose of the Outfall Agreement was to negotiate the use of the outfall for MCWD's assumed participation in the RDP. Now that MCWD will not own or operate the desalination plant, it is likely that performance of the contract will be excused.

---

<sup>55</sup> MCWD Protest, pp. 4-5; Water Plus Protest, p. 4.

<sup>56</sup> A.04-09-019, *Settling Parties' Motion to Approve Settlement Agreement*, Exhibit 1, *Settlement Agreement by and Among California-American Water Company, Marina Coast Water District, Monterey County Water Resources Agency, Monterey Regional Water Pollution Control Agency, Public Trust Alliance, and Surfrider Foundation*, Attachment 2, *Monterey Regional Water Pollution Control Agency And Marina Coast Water District Outfall Agreement*, dated as of February 12, 2010, § 4.9(b)(i).

<sup>57</sup> Svindland Direct, Attachment 5, p. 2.

**A. Performance of the Outfall Agreement Will Likely Be Excused**

Performance of a contract may be excused when: (1) an implied condition of the contract is not met; (2) performance of the contract is impossible; or (3) the purpose of the contract has been frustrated by an unanticipated supervening circumstance to the extent that the value of performance is substantially destroyed.<sup>58</sup> The three defenses are closely related and essentially excuse performance when a necessary assumption of the contract does not exist through no fault of the party seeking to avoid performance.<sup>59</sup> Because California American Water is not a party to the contract between MRWPCA and MCWD, it is unlikely that California American Water has standing to rescind the contract based on any of the above means of invalidation. However, if MCWD were to sue MRWPCA for breach of the Outfall Agreement, MRWPCA could assert the above grounds as a defense.

**1. The Implied Condition of the Outfall Agreement is Not Satisfied**

In *Habitat Trust for Wildlife, Inc. v. City* (2009) 175 Cal.App.4th 1306, 1341, the court excused performance under a contract between a developer and an environmental non-profit advocacy group when a key assumption of the agreement was not satisfied. The developer agreed in its final environmental impact report that to satisfy a mitigation condition it would convey land to “the County of San Bernardino Special District OS-1 or other qualified conservation entity approved by the city.”<sup>60</sup> An environmental advocacy group filed petitions under the California Environmental Quality Act (“CEQA”) claiming that the developer’s designation of mitigating land was vague.<sup>61</sup> In order to prevent a CEQA challenge, the developer entered into an agreement with the advocacy group and a land trust created by the advocacy group, agreeing to convey the mitigating land to the land trust.<sup>62</sup> After the parties entered into the agreement, however, the land trust could not obtain approval as a qualified conservation entity. As a result, the developer’s successor was prohibited by the County from

---

<sup>58</sup> *Habitat Trust for Wildlife, Inc. v. City* (2009) 175 Cal.App.4th 1306, 1335– 1336.

<sup>59</sup> See also *La Cumbre Golf and Country Club v. Santa Barbara Hotel Co.* (1928) 205 Cal. 422, 425–426; *H. Hackfeld & Co., Ltd. v. Castle* (1921) 186 Cal. 53, 57–58.

<sup>60</sup> *Habitat Trust for Wildlife, Inc. v. City* (2009) 175 Cal.App.4th 1306, 1313.

<sup>61</sup> *Id.* at 1334.

<sup>62</sup> *Id.*

conveying mitigating land to the land trust as satisfaction of the mitigation condition.<sup>63</sup>

The advocacy group and the land trust sued the developer and its successor for breach of contract.<sup>64</sup> The court granted the developer's motion for summary judgment claiming the plaintiffs could not establish a breach of contract because the implied condition was not fulfilled.<sup>65</sup> The court found that approval of the land trust as a qualified conservation entity was necessary to fulfill the purpose of the agreement to satisfy the mitigation condition, and therefore, such approval was an implied condition.<sup>66</sup> When the implied condition was not satisfied, the developer had no obligation to perform under the contract.<sup>67</sup>

Similarly, the primary purpose of the Outfall Agreement was to contract for MCWD's RDP Desalination Plant's use of MRWPCA's outfall. As in *Habitat*, the purpose is clear from the face of the contract. The Outfall Agreement is replete with references to the desalination plant described and analyzed in the Commission's FEIR. MRWPCA granted priority use to the RDP Desalination Plant for 34 years. The Outfall Agreement estimated that the outfall would dispose of 12.7 million gallons of brine per day and that MRWPCA would be compensated accordingly, terms that apply specifically to the large RDP Desalination Plant. It makes sense for MRWPCA to give priority use of its outfall for a long period of time to a very large plant that will benefit a significant portion of the population in Monterey. It would be inequitable, however, to permit a small desalination plant that only serves a small portion of the public to monopolize the outfall, a valuable public resource, for a period of 34 years. MCWD's operation of the RDP Desalination Plant is an implied condition of the Outfall Agreement. Since the condition cannot be fulfilled, MRWPCA's performance under the Outfall Agreement is most likely excused.

## **2. Performance of the Outfall Agreement is Impossible**

Performance of a contract is impossible when the subject matter of the contract

---

<sup>63</sup> *Id.* at 1316.

<sup>64</sup> *Habitat Trust for Wildlife, Inc. v. City* (2009) 175 Cal.App.4th 1306, at 1318.

<sup>65</sup> *Id.* at 1333.

<sup>66</sup> *Id.* at 1335–1341.

<sup>67</sup> *Id.* at 1336.

does not exist.<sup>68</sup> “Not only where a specific thing is itself to be sold or transferred, but wherever a contract requires for its performance the existence of a specific thing, the fortuitous destruction of that thing, or such impairment of it as makes it unavailable, excuses the promisor unless he has clearly assumed the risk of its continued existence.”<sup>69</sup> In *Hackfeld*, the court found that because the contract required a specific route and alternate route for shipping goods, that when neither route was possible, it was impossible to perform the contract.

As in *Hackfeld*, because the subject of the Outfall Agreement was MCWD’s ownership and operation of the RDP Desalination Plant, the fact that MCWD will not own or operate the RDP Desalination Plant and cannot force California American Water and MRWPCA to go forward with the RDP, makes the contract impossible to perform. While it is possible that MCWD could own and operate another, much smaller, desalination plant, the Outfall Agreement did not provide use of the outfall for just any desalination plant owned and operated by MCWD.

### **3. The Purpose of the Outfall Agreement has Been Frustrated**

Performance of a contract is excused when “performance of the contract remains possible, but the reason the parties entered the agreement has been frustrated by a supervening circumstance that was not anticipated, such that the value of performance by the party standing on the contract is substantially destroyed, the doctrine of commercial frustration applies to excuse performance.”<sup>70</sup> The court in *Habitat* held that the developer proved frustration when it argued that the essential purpose of its agreement was to satisfy the City’s mitigation condition by transferring mitigation land to the land trust, and that purpose could not be accomplished because the land trust did not qualify to hold the mitigation land.<sup>71</sup>

Similarly, the court in *Federal Leasing Consultants, Inc. v. Lipsett Company, Inc.* (1978) 85 Cal.App.3d Supp. 44, also found a contract unenforceable due to frustration when the subject of the lease, a burglar alarm, was prohibited from use by the United States District Court

---

<sup>68</sup> *H. Hackfeld & Co., Ltd. v. Castile* (1921) 186 Cal. 53, 57–58.

<sup>69</sup> *H. Hackfeld & Co., Ltd. v. Castile* (1921) 186 Cal. 53, 57.

<sup>70</sup> *Habitat, supra*, 175 Cal.App.4th at 1336.

<sup>71</sup> *Id.* at 1336.

because it interfered with government radio signals. In *Johnson v. Atkins* (1942) 53 Cal.App.2d 430, 431, the court held that when buyer and seller had contracted for the shipment of copra from San Francisco to Colombia, and Columbian authorities prevented copra from entering Columbia, the purpose of the contract was frustrated and therefore, unenforceable.

The purpose for MRWPCA and MCWD entering the Outfall Agreement was so that MRWPCA could dispose of brine created by the RDP Desalination Plant. MCWD no longer has the right to own and operate the RDP Desalination Plant as contemplated by the Outfall Agreement. The purpose of the contract has ceased to exist. Therefore, the contract should be avoidable due to frustration.

MRWPCA and MCWD entered into the Outfall Agreement with the purpose of determining the parties' rights as they related to the RDP Desalination Plant and disposal of the brine it produced. Because MCWD will never own and operate the RDP Desalination Plant, the purpose of the Outfall Agreement no longer exists. While MCWD may own and operate a different desalination plant in the future, it would be inequitable for a court to enforce the Outfall Agreement in the absence of MCWD's ownership and operation of the RDP Desalination Plant.

## **VI. THE GROUNDWATER REPLENISHMENT PROJECT WATER RIGHTS ISSUES ARE DIFFERENT BECAUSE CALIFORNIA AMERICAN WATER IS SIMPLY SEEKING TO PURCHASE WATER**

In its Application, California American Water sought authorization to reduce the size of the desalination plant portion of the Monterey Peninsula Water Supply Project from 9.0 million gallons per day ("mgd") to 5.4 mgd and to supplement its supply with water purchased from the Groundwater Replenishment Project if certain conditions are met.<sup>72</sup> The Groundwater Replenishment Project is a joint project between MRWPCA and the Monterey Peninsula Water Management District ("MPWMD").

California American Water is a strong supporter of the Groundwater Replenishment Project and believes that it could be highly beneficial to the Monterey Peninsula.

---

<sup>72</sup> *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*, filed April 23, 2012 ("Application"), p. 1.

The parties involved in the Groundwater Replenishment Project are currently working to address water rights and other project development matters. If the Groundwater Replenishment Project has reached certain milestones by the time California American Water is ready to construct the desalination plant (currently estimated to be the near the end of 2014), and the price of Groundwater Replenishment Project water is reasonable, California American Water will reduce the size of the desalination plant portion of the Monterey Peninsula Water Supply Project. If for some reason the Groundwater Replenishment Project does not go forward, however, California American Water will just proceed with the larger desalination plant.

With respect to the Groundwater Replenishment Project, California American Water is simply seeking the ability to enter into a purchased water contract. Requesting authorization to enter into a purchased water contract is quite different from requesting a CPCN for the Monterey Peninsula Water Supply Project. While the Commission may need to evaluate the water rights issues associated with the Monterey Peninsula Water Supply Project as part of its CPCN process, the same is not necessarily true for the Groundwater Replenishment Project water rights. Nonetheless, in the interest of a full and complete record, MRWPCA will discuss water rights and the Groundwater Replenishment Project in its opening brief. California American Water defers to MRWPCA on this issue.

## **VII. CONCLUSION**

As California American Water, ALJ Weatherford, and numerous parties have noted, time is of the essence. The Monterey Peninsula Water Supply Project will satisfy the State Water Resources Control Board's ("SWRCB") requirements and provide a cost-effective solution based on low-cost financing, government-subsidized loans, tax benefits and use of regulatory opportunities. As discussed above, the Monterey County Ordinance limiting the ownership and operation of a desalination facility in Monterey County to public agencies is preempted by Commission authority and therefore is not an obstacle to the Monterey Peninsula Water Supply Project. Additionally, although multiple parties have raised water rights issues related to the Monterey Peninsula Water Supply Project, these claims do not affect the feasibility

of the Project. With the SWRCB December 2016 deadline looming, California American Water requests that the Commission timely authorize it to implement the Monterey Peninsula Water Supply Project and recover the associated costs in rates.

July 11, 2012

Respectfully submitted,

MANATT, PHELPS & PHILLIPS, LLP

By: /s/ Lori Anne Dolqueist

Lori Anne Dolqueist

Attorneys for Applicant  
California-American Water Company