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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 REPLY TO PROTESTS

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

Attorney 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

June 4, 2012

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CALIFORNIA-AMERICAN WATER COMPANY REPLY TO PROTESTS

Pursuant to Rule 2.6(e) of the Rules of Practice and Procedure of the California Public Utilities Commission ("Commission"), California-American Water Company ("California American Water") hereby submits its reply to the protests filed to the *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"). In this reply, California American Water will respond to the protests filed by the Division of Ratepayer Advocates ("DRA"), LandWatch Monterey County ("LandWatch"), Marina Coast Water District ("MCWD"), and Water Plus.[1] Since there is considerable overlap in the issues raised by the various filing entities, California American Water will respond to the protests by issue, rather than by filer.

As California American Water explained in its Application, the Monterey Peninsula Water Supply Project ("Project") will satisfy the State Water Resources Control Board ("SWRCB") requirement that California American Water find a replacement for approximately 70 percent of its water supply and can be approved, financed, and constructed in time to meet the SWRCB's December 2016 deadline.[2] In light of the urgent need to find a replacement water supply for the Monterey County District, California American Water requests that the

[1] California American will address issues related to the scope of the proceeding and the schedule in its concurrently filed Prehearing Conference Statement.
[2] SWRCB Order 2009-0060, p. 57, *available at* <http://www.waterboards.ca.gov/waterrights/water_issues/programs/hearings/caw_cdo/docs/wro2009_0060.pdf>.

Commission timely authorize it to implement the Monterey Peninsula Water Supply Project and recover the associated costs in rates.

I. CEQA

MCWD, LandWatch and Water Plus all raise issues regarding review of the Monterey Peninsula Water Supply Project under the California Environmental Quality Act ("CEQA"). For example, both MCWD and LandWatch discuss items that they believe should be considered as part of the CEQA analysis.[3] MCWD also claims that in addition to its environmental review of the Monterey Peninsula Water Supply Project, the Commission must conduct the CEQA review of the Monterey Peninsula Groundwater Replenishment Project ("Groundwater Replenishment Project"), a joint project between the Monterey Regional Water Pollution Control Agency ("MRWPCA") and the Monterey Peninsula Water Management District ("MPWMD"), in order to avoid "piecemealing."[4] LandWatch recommends that the Commission postpone consideration of the merits of the Monterey Peninsula Water Supply Project until after the CEQA process is completed.[5] Finally, Water Plus argues that the Environmental Impact Report ("EIR") must be prepared by a county agency, not the Commission.[6]

California American Water supports a full and thorough vetting of the environmental issues and has been working with the Commission's CEQA team to provide assistance and information. As California American Water discussed in its Application, the Monterey Peninsula Water Supply Project is a modified version of the North Marina Project, which the Commission analyzed at a project level of detail in A.04-09-019.[7] It is the

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[3] *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 24, 2012 ("LandWatch Protest"), pp. 3-5; *Marina Coast Water District's Protest of A.12-04-019*, filed May 25, 2012 ("MCWD Protest"), pp. 3-4.

[4] MCWD Protest, p. 5.

[5] LandWatch Protest, p. 3.

[6] *Protest by Water Plus*, filed May 24, 2012 ("Water Plus Protest"), p. 3

[7] *See* D.09-12-017, *Application of California-American Water Company (U210W) for a Certificate of Public Convenience and Necessity to Construct and Operate its Coastal Water Project to Resolve the Long-Term Water Supply Deficit in its Monterey District and to Recover All Present and Future Costs in Connection Therewith in Rates*, 2009 Cal. PUC LEXIS 764.

Commission, not California American Water, who will determine the necessary level of environmental review for the Project.

Contrary to MCWD's claims, however, the Commission is not required to conduct CEQA review of the Groundwater Replenishment Project. The Groundwater Replenishment Project is separate from the Monterey Peninsula Water Supply Project and will be carried out by MRWPCA, not California American Water. California American Water is merely seeking authorization to purchase water from the Groundwater Replenishment Project. CEQA is not triggered for the Commission because approval of a purchased water contract does not involve the granting of a lease, permit, license, certificate, or other entitlement.[8] Furthermore, the Commission would not be a responsible agency with respect to the Groundwater Replenishment Project because it does not have discretionary approval power over the project.[9] Therefore, MCWD's "piecemealing" allegations are unfounded.

Moreover, there is no reason for the Commission to postpone its review of other aspects of the Monterey Peninsula Water Supply Project until the CEQA review is completed, as LandWatch suggests.[10] First, as noted above, the Monterey Peninsula Water Supply Project is a modified version of a project that was already analyzed by the Commission. Second, going forward with California American Water's Application while concurrently conducting CEQA review does not deprive parties of opportunities for comment. The CEQA review process includes multiple opportunities for interested parties to provide input on environmental issues, and California American Water's proposed schedule provides ample time to address other issues. Third, and perhaps most critically, LandWatch's proposal could extend the procedural schedule by half a year or longer, jeopardizing California American Water's ability to meet the SWRCB 2016 deadline. The Commission has previously recognized the "urgent need to find an

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[8] D.86-10-044, *Application of Pacific Gas and Electric Co. for an Order approving an agreement with Kings River Conservation District for the purchase of firm capacity and energy from the Dinkey Creek Hydroelectric Project*, 1986 Cal. PUC LEXIS 642 ("D.86-10-044, 1986 Cal. PUC LEXIS 642"), **16-17.
[9] *Id.*, D.86-10-044, 1986 Cal. PUC LEXIS 642, **17-18; *see* Pub. Resources Code § 21069.
[10] LandWatch Protest, p. 3.

alternative water supply" for California American Water's Monterey County District.[11] Failure to meet the SWRCB December 2016 deadline could have harmful consequences for California American Water, its customers, and the community.[12] Therefore, there is no justification for postponing review of California American Water's Application, as LandWatch suggests.

Finally, Water Plus's claim that the EIR for the Monterey Peninsula Water Supply Project must be conducted by a county agency – not the Commission – is meritless. Unlike the Regional Desalination Project, the Monterey Peninsula Water Supply Project is not a joint project with public agencies – it is being proposed by California American Water alone. In D.03-09-022, the Commission addressed whether it should be the lead agency or whether a county agency should take that role.[13] The Commission correctly concluded that its "broad and specific, statewide authority and responsibility to regulate public utility water companies require that we should assume lead agency status to conduct environmental review."[14] Therefore, the recent Monterey County Superior Court ruling has no bearing on the validity of the existing EIR for a stand-alone California American Water project.

II. ALLEGED OBSTACLES TO THE MONTEREY PENINSULA WATER SUPPLY PROJECT

Although some of the protesting entities made allegations regarding the potential obstacles to the Monterey Peninsula Water Supply Project, their claims are either based on incorrect information or are being addressed by California American Water. These so-called obstacles will not prevent the implementation of the Project.

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[11] D.10-12-016, *In the Matter of the Application of California-American Water Company (U210W) for a Certificate of Public Convenience and Necessity to Construct and Operate its Coastal Water Project to Resolve the Long-Term Water Supply Deficit in its Monterey District and to Recover All Present and Future Costs in Connection Therewith in Rates*, 2010 Cal. PUC LEXIS 548 ("D.10-12-016, 2010 Cal. PUC LEXIS 548"), *35.

[12] D.10-12-016, 2010 Cal. PUC LEXIS 548, **62-63, 250, Findings of Fact ¶ 65.

[13] D.03-09-022, *In the Matter of the Application of California-American Water Company (U 210 W) for a Certificate that the Present and Future Public Convenience and Necessity Requires Applicant to Construct and Operate the 24,000 acre foot Carmel River Dam and Reservoir in its Monterey Division and to Recover All Present and Future Costs in Connection Therewith in Rates*, 1997 Cal. PUC LEXIS 1279 ("D.03-09-022, 1997 Cal. PUC LEXIS 1279"), **15-16.

[14] D.03-09-022, 1997 Cal. PUC LEXIS 1279, *16.

A. Monterey County Ordinance

LandWatch, MCWD, and Water Plus all raise the issue of a Monterey County ordinance[15] that allegedly prohibits private ownership of a desalination facility.[16] While LandWatch and MCWD merely raise it as an issue that could potentially delay the Monterey Peninsula Water Supply Project, Water Plus accuses California American Water of disregarding or acting above the law.[17] This ordinance, however, does not apply to California American Water. In a 2003 memorandum, then-Acting Monterey County Counsel stated that the ordinance was "factually inconsistent," "ambiguous" and "might be preempted" by the Commission's jurisdiction.[18] Jurisdiction over water utilities such as California American Water has been vested exclusively with the Commission, and local ordinances such as the Monterey County ordinance are preempted to the extent they interfere with the Commission's statewide regulation of water utilities.[19] In an April 2012 letter, the Commission's General Counsel concluded that the ordinance is "of no legal validity under settled principles of California law" and would "certainly" be preempted.[20] California American Water is continuing discussions with the County as to the relevancy of this ordinance as it pertains to the Monterey Peninsula Water Supply Project and will address these issues in detail in its briefs, as directed by ALJ Weatherford in his June 1, 2012 ruling.[21]

B. Water Rights

All of the protests raised the issue of whether California American Water must obtain water rights to extract groundwater from the Salinas Valley Groundwater Basin ("Basin"),[22] with MCWD and Water Plus arguing that the lack of such rights would doom the

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[15] Monterey County Ordinance 10.72.030(B).
[16] Land Watch Protest, p. 7; MCWD Protest, p. 4, Water Plus Protest, pp. 3, 8.
[17] Water Plus Protest, p. 8.
[18] This memorandum was inadvertently omitted from Attachment 7 to the Direct Testimony of Richard C. Svindland when it was served with the Application. California American Water has attached it to this reply. It is also now included in the copy of the testimony available on California American Water's website at http://www.watersupplyproject.org/.
[19] *Id.*
[20] *Direct Testimony of Richard C. Svindland*, dated April 23, 2012 ("Svindland Direct"), Attachment 7.
[21] *Administrative Law Judge's Ruling*, filed June 1, 2012 ("June 1, 2012 Ruling"), p. 3.
[22] *Protest of The Division of Ratepayer Advocates*, filed May 25, 2012 ("DRA Protest"), p. 5; LandWatch Protest, pp. 4, 7; MCWD Protest, p. 4; Water Plus Protest, p. 4.

Project. However, as California American Water will discuss in greater detail in its briefs, the Project does not require water rights for the pumping, treatment and beneficial use of ocean water. To the extent the Project may capture native groundwater, there is no "appropriation" of water from the Basin and no water rights are required because the Project will return any groundwater that originates in the Basin to the Basin for the benefit of water users in the Basin

C. Acquisition of Land and Easements

California American Water explained in its Application that it is in the process of securing an approximately 46-acre parcel of land for the proposed desalination plant, as well as easements on an approximately 376-acre parcel of land for the slant intake wells.[23] In their protests, DRA and MCWD express concern that these acquisitions could result in delay or increased costs.[24] California American Water has, however, included appropriate estimates in it Application to cover the cost of land and easements.[25] With respect to the land for the desalination plant, California American Water expects to conclude its negotiations in due time and estimates that it will be able to obtain the parcel in accordance with our projected estimates. As for the parcel for the wells, the Commission's CEQA team has recently completed the biological survey of this area,[26] which has allowed California American Water to begin siting the easements. Based on this progress, California American Water does not foresee these acquisitions hindering the implementation of the Monterey Peninsula Water Supply Project.

D. Outfall Capacity

As California American Water explained in its Application, it 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.[27] MCWD and Water Plus claim that MCWD has a senior right to this outfall capacity, which could prevent California American Waters use of the

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[23] Application, p. 7; Svindland Direct, p. 9.
[24] DRA Protest, p. 4; MCWD Protest, p. 4.
[25] Svindland Direct, p. 9, Attachment 4.
[26] The site visit occurred on May 16-17, 2012.
[27] Application, pp. 5-6.

MRWPCA outfall.[28] As directed by ALJ Weatherford, California American Water will address this issue in more detail in its briefs and will demonstrate that MCWD's claim does not prevent California American Water's proposed use of the outfall. Briefly, the Outfall Agreement that provides the basis for this claim, however, was related to the Regional Desalination Project. Because the Water Purchase Agreement and related Regional Desalination Project agreements have been terminated,[29] the intended purpose for the Outfall Agreement is frustrated as a matter of law. Moreover, based on California American Waters technical analysis, the outfall has sufficient capacity to accommodate MRWPCA average daily wastewater flows, the brine discharge from the Monterey Peninsula Water Supply Projects desalination facility, and the original MCWD Regional Desalination Project brine discharge (even though the Regional Desalination Project will not be constructed).

E. Financing

LandWatch, MCWD, and Water Plus all question California American Water's ability to obtain financing from the State Revolving Fund, due to California American Water's status as a private company.[30] As California American Water discussed in its Application, however, the Monterey Peninsula Water Supply Project would qualify as a non-point source for water pollution control.[31] As such, the Project is eligible for State Revolving Fund loans under the non-point source funding allowances in Clean Water Act Section 603(c)(2) or (c)(3) (33 U.S.C. § 1383(c)(2) and (3)). Unlike other sections of the Clean Water Act, nothing in subsections (c)(2) or (c)(3) restrict funding to a municipal project.

The State Revolving Fund program is implemented in California by the Division of Financial Assistance within the SWRCB, with oversight by the United State Environmental Protection Agency ("EPA"). In discussions and correspondence, both the SWRCB and the EPA have confirmed that that the Monterey Peninsula Water Supply Project preliminarily meets the

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[28] MCWD Protest, pp. 4-5; Water Plus, p. 4.
[29] A.04-09-019, *Status Report of California-American Water Company*, filed March 1, 2012, pp. 2-3.
[30] LandWatch Protest, p. 5; MCWD Protest, p. 5; Water Plus Protest, pp. 6-7.
[31] Application, p. 14.

criteria for State Revolving Fund loans. California American Water is continuing to work with Division of Financial Assistance staff to obtain this financing.

III. GROUNDWATER REPLENISHMENT PROJECT

Both LandWatch and Water Plus question California American Water's commitment to the Groundwater Replenishment Project.[32] In its Application, California American Water sought authorization to reduce the size the desalination plant portion of the Monterey Peninsula Water Supply Project from 9.0 million gallons per day ("mgd") to 5.4 mgd and supplement with water purchased from the Groundwater Replenishment Project, if the Groundwater Replenishment Project meets certain timing milestones and if the cost of the water is reasonable.[33] The Groundwater Replenishment Project will create a drought-proof source of supply by taking the effluent from MRWPCA's plant, filtering it through a new advanced water treatment plant, and injecting the highly treated product water into the Seaside Basin Aquifer, where it would be diluted and stored.[34]

California American Water is a strong supporter of the Groundwater Replenishment Project and believes that it could be highly beneficial to the Monterey Peninsula, which is why it agreed to collaborate with MRWPCA and MPWMD to develop the Groundwater Replenishment Project. California American Water cannot ignore, however, its legal obligation to meet the SWRCB December 2016 deadline, or the requirement that its rates be just and reasonable. That is why California American Water's proposal to reduce the size of its proposed desalination plant is contingent on the Groundwater Replenishment Project reaching certain milestones before construction begins on the desalination plant (currently estimated to be near the end of 2014) and on the cost of product water being reasonable. These contingencies should not be construed as lack of support for the Groundwater Replenishment Project but rather assurances that California American Water's involvement will not undermine its ability to meet its legal obligations.

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[32] LandWatch Protest, p. 6; Water Plus Project, pp. 5-6.
[33] Application, pp. 5-6, 11.
[34] Application, pp. 5-6.

IV. RATEMAKING

DRA was the only party to address California American Water's surcharge proposal directly.[35] DRA's main comment was that it would review and analyze the proposed rate recovery mechanisms over the course of the proceeding. DRA did recommend, however, that costs related to the Regional Desalination Project be addressed in A.04-09-019, not in this proceeding.[36] However, it was never California American Water's intention that the costs related to the Regional Desalination Project would be reviewed as part of this proceeding.[37] This was confirmed by ALJ Weatherford in his June 1, 2012 ruling, in which he stated that any unresolved issues related to the Regional Desalination Project would not be addressed in this proceeding.[38] In light of the statements in DRA's protest and ALJ Weatherford's ruling, California American Water has removed the sections of David Stephenson's testimony that address specific costs from the Regional Desalination Project. Although the costs themselves will not be addressed in this proceeding, California American Water still requests the ability to track and recover Regional Desalination Project costs separately from Monterey Peninsula Water Supply Project costs.[39]

DRA also appears to recommend that California American Water track the costs of the test well and other pre-construction costs a new memorandum account, capped at $5 million.[40] It is unclear whether this $5 million is for just the test well or all pre-construction costs. Moreover, California American Water is not seeking a new memorandum account. As noted in the Application and supporting materials, California American Water will track the cost of the test well and other pre-construction costs in the existing memorandum account.[41] If the Commission approves California American Water's application, it will include the costs of the test well in the construction cost of the Monterey Peninsula Water Supply Project and recover

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[35] DRA Protest, pp. 9-10.
[36] DRA Protest, p. 9.
[37] Application, p. 15.
[38] June 1, 2012 Ruling, p. 2.
[39] Application, pp. 14-16; *Direct Testimony of David P. Stephenson*, dated April 23, 2012 ("Stephenson Direct"), pp. 12-14.
[40] DRA Protest, p. 9.
[41] Application, p. 15; Stephenson Direct, pp. 14-15.

them as part of the overall costs in rates. If for some reason the Monterey Peninsula Water Supply Project does not go forward, California American Water would seek to recover the test well costs, as well as other pre-construction costs, through Surcharge 1.

As discussed in the Application and supporting documents, California American Water requested an interim ruling on the test well, since it is critical that California American Water move forward as soon as possible. The test well facilities will provide important water quality data for design of the plant and assess individual well capacities and salinity levels and will assist California American Water in moving forward with the Monterey Peninsula Water Supply Project. The initial data from the test well may also assist the Commission in its CEQA review. No party directly opposed the test well, and others, such as DRA, recognized the value of it.[42] Therefore, in order to ensure the expeditious development of the Monterey Peninsula Water Supply Project, California American Water requests a ruling confirming the propose ratemaking treatment for the test well facilities at the prehearing conference or as soon as possible thereafter.

V. ALTERNATIVE PROPOSALS

MCWD, Water Plus, and LandWatch all suggest alternatives or modifications to the Monterey Peninsula Water Supply Project. For example, LandWatch suggests that California American Water seek a public partner for the Project.[43] While California American Water welcomes the relevant input and participation of public agencies, and will work with them to address any requirements or permitting issues, it believes that the stand-alone Monterey Peninsula Water Supply Project is the best option to meet the SWRCB December 2016 deadline.

MCWD, unsurprisingly, continues to suggest that California American Water pursue the defunct Regional Desalination Project.[44] As California American Water explained in its Application and elsewhere, however, the Regional Desalination Project is no longer viable

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[42] DRA Protest, p. 9.
[43] Land Watch Protest, pp. 5, 7.
[44] *See* MCWD Protest.

and would not allow California American Water to meet the SWRCB December 2016 deadline.[45] Moreover, ALJ Weatherford's June 1, 2012 ruling, in which he denies MCWD's motion to dismiss California American Water's Application, makes it clear that the purpose of this proceeding its to evaluate the merits of the Monterey Peninsula Water Supply Project – not rehash issues related to the Regional Desalination Project.[46]

Water Plus suggests the Nader Agha-sponsored People's Moss Landing Desalination Project as an alternative solution to the long-term water supply issues facing the Monterey County District.[47] California American Water's review of this project to date, however, indicates that it is unsuitable for a variety of reasons. Water Plus goes on to argue, however, that since Mr. Agha is proposing an alternate project, the Commission no longer has jurisdiction to decide the merits of California American Water's proposal.[48] This is clearly untrue, as the Legislature granted the Commission broad, general powers to regulate public utilities. In particular, the Commission has specific jurisdiction to regulate the service of water utilities with respect to the health and safety of that service[49] and the power and obligation to determine that any rate is just and reasonable.[50] Additionally, the Commission has the authority to "supervise and regulate every public utility in the State and do all things which are necessary and convenient in the exercise of such power and jurisdiction."[51] The Commission's jurisdiction over California American Water and the proposed Monterey Peninsula Water Supply Project is not affected by Mr. Agha's alternate proposal.

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[45] California American Water discussed these issues in multiple pleadings in A.04-09-019: *California-American Water Company Compliance Filing - Mediation Update*, filed January 18, 2012, pp. 1-2; *Status Report of California-American Water Company*, filed March 1, 2012, pp. 2-3; *California-American Water Company Compliance Filing*, filed March 1, 2012, pp. 2-5; *California-American Water Company Response to the Separate Status Report of Marina Coast Water District*, filed March 15, 2012, pp. 2-9. Although California American Water, MCWD and the Monterey County Water Resources Agency participated in mediation regard the Regional Desalination Project for a total of almost five months, a variety of obstacles remained, including failure to obtain test well permits, water rights lawsuits, lack of financing, and a ruling from the Monterey County Superior Court that the EIR was not valid for use by MCWD as lead agency.
[46] June 1, 2012 Ruling, pp. 2-3.
[47] Water Plus Protest, pp. 8, 9.
[48] Water Plus Protest, p. 8.
[49] Pub. Util. Code §§ 451, 761, 739.8, 768, 770(b).
[50] Pub. Util. Code §§ 451, 454.
[51] Pub. Util. Code § 701.

In preparing its proposal, California American Water evaluated multiple alternatives for solving its long-term water supply constraints. As California American Water discussed in its Application and supporting testimony, it developed the Monterey Peninsula Water Supply Project as a flexible, cost-effective, and timely way to meet the SWRCB's requirements. The Monterey Peninsula Water Supply Project will provide the consistent, reliable water supply necessary to cease diversion of 7,602 acre-feet annually from the Carmel River and can be approved, financed, and constructed by December 2016, as required by the SWRCB.

VI. CONCLUSION

As discussed above and in California American Water's Application, the Monterey Peninsula Water Supply Project can be approved, financed, and constructed in time to meet the SWRCB's deadline, will satisfy the SWRCB's requirements, and provides a cost-effective solution based on low-cost financing, government-subsidized loans, tax benefits and use of regulatory opportunities. With the 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.

June 4, 2012

Respectfully submitted,

MANATT, PHELPS & PHILLIPS, LLP

By:_____
Lori A. Dolqueist

Attorneys for Applicant
California-American Water Company

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Monterey County Counsel Memorandum

MEMORANDUM

OFFICE OF THE COUNTY COUNSEL
COUNTY OF MONTEREY

DATE: April 1, 2003

TO: Honorable Chair and Members of the Board of Supervisors

FROM: David Nawi
Acting County Counsel

SUBJECT: Proposed Desalination Facility of Moss Landing

SUMMARY

At its meeting of March 18, 2003, the Board requested information from County Counsel regarding issues related to the permitting, regulation and environmental review of a desalination facility proposed to be located in Monterey County. Our initial analysis is set forth below. In summary:

1. Both the County and the California Public Utilities Commission have authority with respect to the project. Because the Commission is a constitutionally created state agency, its authority is generally paramount.

2. The applicable provisions of the County ordinance relating to ownership and operation of desalination facilities by public entities are ambiguous and subject to interpretation by the Board.

3. Various considerations affect the determination of lead agency for purposes of environmental review under the California Environmental Quality Act. If the County is not lead agency, it would participate in the environmental review process as a responsible agency.

BACKGROUND

California-American Water Company (Cal-Am) filed in February an application with the California Public Utilities Commission (Commission or PUC) for authorization to develop a new long-term water supply through construction and operation of a desalination plant and pipeline, in conjunction with use of underground storage areas (the Project). The Project would be located entirely in Monterey County.

The Monterey County Water Resources Agency (MCWRA) and the County have identified concerns regarding the Project based on information available at the early stages of the PUC process. MCWRA and the County are concerned that, as presently defined, the Cal-Am Project would not be able to accommodate both Cal-Am's proposal and the need for new sources of water MCWRA and the County have identified. They are also concerned about the potential environmental impacts of the Project. To provide information on potential means to address these concerns as the Project moves forward, this memorandum presents County Counsel's initial analysis of issues that have been identified regarding the permitting and environmental review of the Project.

Pursuant to an order of the PUC dated March 12, 2003, Cal-Am is to file by April 1 additional information regarding permitting issues, and parties may comment on Cal-Am's submissions, including the issue of CEQA lead agency designation, by April 11. We anticipate the potential of further analysis after receipt and review of Cal-Am's submission.

PUC AND COUNTY PERMITTING AUTHORITY

The PUC has jurisdiction over the Project pursuant to provisions of the California Public Utilities Code specifying that no water corporation may begin the construction of a line, plant, or system without first obtaining a certificate of public convenience and necessity (CPCN) from the Commission. (Pub. Util. Code sec. 1001.) The County also has permitting authority over the Project because the Project would be within the County in the Coastal Zone on the property southeast of the Dolan Road/Highway1 intersection,. Our understanding is that the project would be commonly known as the Kaiser property, which is mainly zoned for High Industrial uses. It also contains a portion of land zoned for Resource Conservation. Authority to issue permits for development in the Coastal Zone was granted to the County through the California Coastal Commission certification of County's Local Coastal Plan. (Pub. Res. Code sec. 30519(a).) The placement of a pipeline from the proposed plant to Cal-Am's Monterey Division service area could require additional Coastal Development Permits from the County.

The PUC is an agency of the State, created by the California Constitution. Consequently, its powers are superior to those of local entities, such as the County. The California Constitution provides that "[a] city, county, or other body may not regulate matters over which the Legislature grants regulatory power to the Commission."[1] The power of a city or county to "make and enforce within its limits all local, police, sanitary, and other regulations" is specifically limited to such regulations as are "not in conflict with general laws."[2] Thus, it follows that in the event of a conflict between an action by a county and a lawful order of the Commission, the Commission order prevails.[3] "[T]he commission has been held to have

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1 Cal. Const. Art. XII, § 8.
2 Cal. Const. Art. XI, § 7.
3 *Harbor Carriers, Inc. v. City of Sausalito*, (1975) 46 Cal.App. 3d 1 773, 775.

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."[4]

The California Constitution, in Article XII, § 8, and Public Utilities Code sections 2901 through 2907 appear to authorize local authorities to exercise a measure of regulatory power over public utilities notwithstanding state preemption. State law explicitly states that a local agency is not required to surrender to the PUC "its powers of control to supervise and regulate the relationship between a public utility and the general public in matters affecting the health, convenience, and safety of the general public." (Pub. Util. Code sec. 2902.) However, these state statutes do not provide absolute statements outlining the powers and limitations on local zoning regulation of public utilities.

In general, courts have held that, where a local agency regulates matters over which the PUC has regulatory power, state law impliedly preempts local legislation because regulation of utilities is a mater of statewide concern. For example, in *Harbor Carriers*, the certificate of public convenience and necessity (CPCN) issued by the Commission authorized the respondent to conduct a common carrier service, by ferry, between San Francisco and Sausalito. A terminal and docking facility were necessary for operation of the service. The city of Sausalito tried to apply its zoning ordinance to prevent construction of a terminal. 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." The court further concluded that a city terminal site was "necessarily contemplated by the commission's certificate authorizing service" and ordered the city to afford the opportunity for a reasonable terminal site.[5]

Applying these principles and precedent to the Cal-Am Project, 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. However, the County may include appropriate conditions relating to matters of local concern in any land use authorization. An analysis of the precise scope of the County's permitting authority and of the conditions it may impose must await further information regarding the Project as it develops and the terms of a CPCN that the PUC may issue.

Any permits issued by the County governing aspects of the Project within the Coastal Zone would be subject to appeal to and review by the Coastal Commission. Additionally, the Coastal Commission has permitting authority for development in tidelands, submerged lands, or on public trust lands, whether filled or unfilled, lying within the Coastal Zone. (Pub. Res. Code sec. 30519(b).) In the case of the proposed desalinization plant, this

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4 Id. (quoting *Orange County Air Pollution Control District v. Public Utilities Commission*, (1971) 4 Cal. 3d 945, 950-951).

5 *Id.* at 775-776.

authority would likely apply to the placing of intake and outlet pipes below mean high tide in the Moss Landing area. If federal funding or federal permitting is needed to implement the project within the coastal zone, the Coastal Commission will likely have to undertake Federal consistency review pursuant to the Coastal Zone Management Act.

COUNTY ORDINANCE REGARDING DESALINIZATION FACILITIES

In addition to the above land use permits, the County's "Desalinization Treatment Facility" ordinance (Monterey County Code, chapter 10.72) requires an applicant for a desalinization facility to obtain a permit from the Director of Environmental Health to construct and operate the facility. The Board has asked for County Counsel's guidance as to whether the ordinance requires the facility to be owned and operated by a public entity. County Counsel's view is that the ordinance is ambiguous and therefore subject to the Board's interpretation on this point.

Section 10.72 .030 provides, in relevant part:

All applicants for an operation permit as required by Section 10.72.010 shall:

A. Provide proof of financial capability and commitment to the operation, continuing maintenance replacement, repairs, periodic noise studies and sound analyses, and emergency contingencies of said facility. . . . For regional desalinization projects undertaken by any public agency, such proof shall be consistent with financial market requirements for similar capital projects.

B. Provide assurances that each facility will be owned and operated by a public entity.

Subsection "B," taken alone, appears to require a public entity to own and operate the facility.[6] However, the section of the ordinance that sets forth the basic permit requirement, section 10.72.010, does not restrict potential permittees to public entities. Section 10.72.010 states that "no person, firm, water utility, association, corporation, organization, or partnership, or any city, county, district, or any department or agency of the State shall commence construction of or operate any Desalinization Treatment Facility... without first securing a permit to construct and a permit to operate said facility."

The above two provisions appear facially inconsistent, thus presenting a question of interpretation. The Board could read subsection B to restrict owners and operators of desalination facilities to public entities in all cases. Alternatively, reading the requirements of

[6] It is possible that the Board could interpret the phrase "public entity" in the ordinance to apply to Cal-Am, even though Cal-Am is a privately-owned for profit entity that would not be considered a public entity in most contexts. The interpretation would rest on Cal-Am's status as a regulated public utility. However, if this interpretation were accepted, the provision in Section 10.72.030.B would be rendered meaningless.

subsection 10.72.030.B in light of the broader provision of section 10.72.010, the Board could interpret the ordinance to mean that the operator must either be a public entity as provided in subsection B, or demonstrate sufficient financial capability and commitment to operate and maintain the facility as provided in subsection A. Under these provisions, the Director of Environmental Health has issued a permit to a non-profit organization after it demonstrated it had the financial capacity to operate its proposed desalinization facility.

Relevant to this issue is the potential, based on the principles set out above regarding the effect of PUC jurisdiction on local authority, that if the PUC authorizes the Cal-Am desalination project, the County might be preempted from using a "public entity" requirement to deny Cal-Am a permit to operate the facility.

Further evidence or analysis may help clarify this issue. The Board need not reach a conclusion regarding its interpretation of the ordinance at this time. When it does, it may wish to clarify the ordinance through amendment.

CEQA LEAD AGENCY

The CEQA Guidelines set forth criteria for determining which agency will be the lead agency where two or more public agencies will be involved with a project. Where a project is to be carried out by a non-governmental person or entity, such as Cal-Am, the lead agency is to be the agency with the greatest responsibility for supervising or approving the project as a whole.[7] Further, the lead agency typically will be the agency with general governmental powers, such as a city or county, rather than an agency with a single or limited purpose, such as an air pollution control district.[8] Finally, where more than one public agency equally meet these criteria, the agency which will act first on the project in question shall be the lead agency.[9]

The Commission's rules provide that "the Commission is the lead agency for the following stationary utility projects: . . . (C) new and noncontiguous utility facility projects (independent of subdivisions) . . . (F) proceedings directly related to new construction of utility facilities."[10] Both of these categories would appear to apply to the Project. However, the Commission does not always assume the lead agency role in such cases. (For example, the Monterey Peninsula Water Management District was the CEQA lead agency for Cal-Am's Carmel River Dam application.)

The County has the ability to seek designation as lead agency if it so desires. If the PUC rather than the County assumes the role of lead agency, the County would participate in

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[7] CEQA Guidelines section 15051(b)

[8] CEQA Guidelines section 15051(b)(1). The CPUC likely would not be viewed as a single or limited purpose agency, given its broad authority vis-à-vis regulation of public utilities and its utility project siting authority.

[9] CEQA Guidelines section 15051(c). Here, the CPUC would probably issue its CPCN before the County issues a land use approval.

[10] Commission Rule 17.1(i).

the CEQA process as a responsible agency. A responsible agency has a more limited role in the CEQA process than the lead agency and generally speaking is limited to areas within the scope of its regulatory authority. (See CEQA Guidelines Sec. 15096.)

The County may also consider pursuing an agreement with the PUC pursuant to which the PUC and the County would act as joint lead agencies. As a joint lead agency the County would have a much more significant role in the CEQA process.

The County will have the opportunity to address the CEQA lead agency issue in detail in its April 11 comments addressing Cal-Am's April 1 filing.

David Nawi

DAVID NAWI
Acting County Counsel

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