

Decision 10-08-008 August 12, 2010

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

In the Matter of the Application of  
California-American Water Company (U210W)  
for an Order Authorizing the Transfer of Costs  
Incurred in 2008 for its Long-Term Water  
Supply Solution for the Monterey District to its  
Special Request 1 Surcharge Balancing Account.

Application 09-04-015  
(Filed April 16, 2009)

**DECISION APPROVING PARTIAL SETTLEMENT AGREEMENT AND,  
WITH MODIFICATIONS, REIMBURSEMENT AGREEMENT**

**1. Summary**

By today's decision, we approve a Partial Settlement Agreement entered into by the California-American Water Company (Cal-Am) and the Division of Ratepayer Advocates. We find that the Partial Settlement Agreement is reasonable in light of the whole record, consistent with the law, and in the public interest, consistent with the requirements of Rule 12.1(d) of the Commission's Rules of Practice and Procedure.

Our approval of the Partial Settlement Agreement authorizes Cal-Am to recover \$5,095,213 for all Coastal Water Project costs incurred through December 31, 2008. Cal-Am will recover these costs from ratepayers through the Special Request 1 Surcharge Balancing Account authorized in Decision (D.) 06-12-040. The Settlement Agreement adopted today does not affect Cal-Am's ability to recover preconstruction costs incurred after December 31, 2008 and tracked in the memorandum account approved in D.03-09-022.

This decision also addresses the issues raised in the Joint Motion for Approval of a Reimbursement Agreement, filed on February 26, 2010 by Cal-Am, Marina Coast Water District (MCWD), and Monterey County Water Resources Agency (MCWRA). The Reimbursement Agreement is designed to allow Cal-Am to advance funds to MCWD and MCWRA to allow their continued participation in pursuing the proposed Regional Project, at issue in Application 04-09-019. As set forth in Exhibit A to the Reimbursement Agreement, the proposed funding will not exceed \$4,376,497 million and the funds are anticipated to be repaid with interest, assuming the proposed Regional Project is approved and built. We approve the Reimbursement Agreement with certain clarifications, as we discuss below.

## **2. Background**

Decision (D.) 03-09-022 authorized California-American Water Company (Cal-Am) to establish a memorandum account to record costs associated with preliminary engineering studies, environmental studies, analysis of necessary permitting requirements, and development of cost estimates for the Coastal Water Project. D.06-12-040 authorized the Special Request 1 Surcharge Balancing Account to allow recovery of prudently incurred preconstruction costs.

On April 16, 2009, Cal-Am filed Application (A.) 09-04-015 requesting authorization to transfer a total of \$5,620,977 in preconstruction costs for the Coastal Water Project that have been tracked in the authorized memorandum accounts to its Special Request 1 Surcharge Balancing Account for recovery from its ratepayers. In A.04-09-019, Cal-Am has applied for a certificate of public convenience and necessity (CPCN) to construct and operate a desalination plant and associated facilities proposed to address long-term water supply problems on the Monterey Peninsula. The proposed project and the alternatives studied in

the Final Environmental Impact Report (FEIR) are known as the Coastal Water Project.

As we discussed in D.09-12-017, which certifies the FEIR in A.04-09-019, the water supply deficit on the Monterey Peninsula is long-standing. Cal-Am has been subject to an order by the State Water Resources Control Board (SWRCB) since 1995 to cease diverting water from the Carmel River and to find an alternative supply of 10,730 acre-feet per year (afy) of water.<sup>1</sup> In 2006, the Monterey County Superior Court established physical limitations to various users' water allocations to reduce the drawdown of the Seaside Basin aquifer and to prevent additional seawater intrusion. Cal-Am's allocation from the Seaside Basin will be reduced over time. Also, in 2006, the Monterey Peninsula Water Management District (MPWMD) updated the total demand in Cal-Am's service territory. The replacement water supply required to meet the updated demand is 12,500 afy. On October 20, 2009, the SWRCB issued Order WR 2009-0060, a Cease and Desist Order that requires Cal-Am to take additional measures to reduce its diversions from the Carmel River and to terminate all such diversions no later than December 31, 2016.

On August 4, 2009, the Division of Ratepayer Advocates (DRA) filed a motion to strike portions of Cal-Am's testimony and to exclude certain issues from this proceeding. Cal-Am filed its response on August 19, 2009. The Scoping Memo Ruling, issued on September 3, 2009, granted DRA's motion and eliminated from the scope of this proceeding the recovery of legal costs incurred by Cal-Am in contesting the Draft Cease and Desist Order issued by the SWRCB

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<sup>1</sup> Order WR 95-10.

regarding compliance with its Order WR 95-10.<sup>2</sup> The Scoping Memo Ruling also excluded the issues related to delays in the issuance of the FEIR in A.04-09-019 from the scope of this proceeding.

On December 18, 2009, DRA served its Audit Report on California American Water Company's Coastal Water Project 2008 Preconstruction Costs, recommending that Cal-Am's request be reduced by \$5,583 due to expense recording errors and legal fees that DRA states are unreasonable.<sup>3</sup> Settlement negotiations ensued in January and February 2010.

On February 26, 2010, Marina Coast Water District (MCWD) and Monterey County Water Resources Agency (MCWRA, together known as the Local Agencies) moved to intervene in this proceeding. On the same date, Cal-Am and the Local Agencies filed and served a Joint Motion requesting expedited approval of a Reimbursement Agreement. The proposed agreement would allow Cal-Am to advance funds to the Local Agencies in order for MCWD and MCWRA to continue to participate in the development and negotiations related to the Regional Project, proposed as an alternative to the proposed Moss Landing Project in A.04-09-019. On March 5, 2010, DRA timely filed its opposition to the motions. MPWMD also timely moved for party status and opposed the Joint Motion.<sup>4</sup>

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<sup>2</sup> SWRCB issued a notice of its Proposed Cease and Desist Order on January 15, 2008. We issued Resolution W-4824 on April 8, 2010, which allowed Cal-Am to establish a memorandum account to track costs incurred in addressing the SWRCB Cease and Desist Order.

<sup>3</sup> Exhibit 4 at 3-2.

<sup>4</sup> On March 31, 2010, MPWMD filed and served an amended response to the Joint Motion, removing its opposition, noting that a settlement agreement had been reached

*Footnote continued on next page*

The assigned Commissioner and Administrative Law Judge (ALJ) issued an Amended Scoping Memo and Ruling that granted the motions to intervene, allowed Cal-Am to track certain costs related to the proposed Reimbursement Agreement in the Coastal Water Project Memorandum Account, and required Cal-Am to track related administrative and legal costs with specificity. On March 12, 2010, parties filed and served a Motion for Approval of Partial Settlement Agreement and requested that the testimony be identified and received into evidence. The ALJ received the exhibits into the record by ruling issued on June 14, 2010.

Cal-Am, the Local Agencies, and DRA timely filed and served concurrent opening and reply briefs.

### **3. Partial Settlement Agreement**

Other than the proposed Reimbursement Agreement, the Settling Parties agree on all the disputed issues in the Application including:

1. Settling Parties agree that the Commission should authorize Cal-Am to transfer \$5,095,213 in preconstruction costs incurred through year-end 2008 for the Coastal Water Project to the Special Request 1 Surcharge Balancing Account.
2. Settling Parties agree that Cal-Am's total request for recovery should be reduced by \$5,583 for invoice recording errors and unreasonable legal fees.

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among Cal-Am, the Local Agencies, and MPWMD regarding the Regional Project in A.04-09-019. However, because MPWMD's Board did not approve the proposed settlement agreement at a special meeting on April 5, 2010, MPWMD essentially renewed its opposition to the Reimbursement Agreement on April 7, 2010.

3. Settling Parties agree that the proposed recovery reflects the reduction of \$520,181 in legal fees, stricken in the Scoping Memo Ruling, in response to DRA's motion.

**4. The Partial Settlement Agreement is in the Public Interest, Consistent with the Law and Reasonable in Light of the Whole Record**

The Partial Settlement Agreement was reached after DRA conducted a thorough review and audit of the 2008 preconstruction costs. The agreement represents a reasonable resolution of the narrow dispute between Cal-Am and DRA regarding the Coastal Water Project preconstruction costs. DRA reviewed the documents reflecting Cal-Am's 2008 costs and found most of them to be reasonable.

We agree that the agreed-upon 2008 preconstruction costs were reasonably and properly incurred in the pursuit of a long-term water supply solution on the Monterey Peninsula. We find that the Partial Settlement Agreement also complies with our prior decisions addressing the Coastal Water Project preconstruction costs.

We find that the proposed Partial Settlement Agreement is in the public interest both because the agreed-upon costs are reasonable and because it will avoid potentially costly litigation. The disputed amounts in question are *de minimus* and it is certainly preferable that parties develop their own mutually-agreeable solution regarding the relatively minor disputed amounts. There is no need for the Commission or the parties to invest further time and resources in litigation. For all of the foregoing reasons, we grant the Settling Parties' Motion and adopt the Partial Settlement Agreement as proposed.

## **5. Joint Motion for Approval of Reimbursement Agreement**

The moving parties state that approval of the proposed Reimbursement Agreement would allow Cal-Am to record the funds advanced to the Local Agencies and the revenues repaid by the Local Agencies (with interest) in the Special Request 1 Surcharge Balancing Account. The funds advanced would not exceed \$4.3 million and, assuming the proposed Regional Project is approved and built, would be repaid with interest. The moving parties explain that they have been working together collaboratively to develop a workable regional solution to the water supply deficit, but the Local Agencies cannot allocate additional resources to this effort because of cash flow concerns. They therefore seek authority for Cal-Am to advance funds to cover project-related costs from February 9, 2010 (the date this issue was first raised at the Status Conference held in A.04-09-019) until the Local Agencies are able to issue bonds, or December 31, 2010, whichever occurs first, when the monies would be repaid. According to the Joint Motion, these repayments will cancel out the funds advanced under the Reimbursement Agreement. If there are remaining costs, however, the moving parties would expect these costs to be subject to reasonableness review and would then request recovery from Cal-Am's ratepayers. Under the provisions of the proposed Water Purchase Agreement in the Settlement Agreement in A.04-09-019, the financing that would be used to repay Cal-Am would become part of the capital costs of the Regional Project and that debt service would be funded by Cal-Am's ratepayers.<sup>5</sup> If the Regional Project is not built for some

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<sup>5</sup> The Water Purchase Agreement under consideration in A.04-09-019 is quite complicated and is not being considered here. As proposed, to the extent MCWD takes permanently allocated water, it will also contribute to the debt service coverage.

reason, the costs of the proposed Reimbursement Agreement would remain the responsibility of Cal-Am's ratepayers.

As described in Exhibit B to the motion, the scope of work is limited to time-critical tasks associated with work related to permitting and design of test wells and preparation of environmental documentation required to obtain federal or state funding.<sup>6</sup> The scope of work also includes MCWD and MCWRA administrative, consultant, and legal support services "required to provide continued development of the Monterey District water supply solution as referenced in California Public Utilities Commission (CPUC) Application No. 04-09-019."<sup>7</sup>

## **6. Responses to Motion**

DRA opposes both the motion to intervene and the motion for approval of the Reimbursement Agreement. DRA maintains that it is not proper for Joint Parties to request approval of this approach in this proceeding and instead recommends that Joint Parties file a petition to modify D.03-09-022. DRA also states that neither the assigned Commissioner nor the assigned ALJ has the authority to approve the requested Reimbursement Agreement. DRA also objects to ratepayer funding of this kind of speculative arrangement and recommends that shareholders bear these costs, if Cal-Am wishes to proceed. DRA explains that it would support a petition to modify D.03-09-022 if costs were limited to the development costs associated with test wells and related permitting and property acquisition.

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<sup>6</sup> Joint Motion, Exhibit B at 1.

<sup>7</sup> *Id.*

MPWMD also objects to the Joint Motion and requests clarification of the Commission's authority to approve such an arrangement. MPWMD agrees with DRA that Cal-Am's ratepayers should not be at risk for the administrative and legal costs and requests that the Commission clarify the details of any such arrangement, if approved.

## **7. Discussion Regarding Amended Scope**

In the Joint Amended Scoping Memo and Ruling, the assigned Commissioner and ALJ granted the Motions Requesting Leave to Intervene, granted party status to MCWD, MCWRA, and MPWMD, and found that the issues raised are reasonably pertinent to this proceeding, pursuant to Rule 1.4(b) of the Commission's Rules of Practice and Procedure (Rules).

As the Amended Scoping Memo explained, parties have arrived at an unusual juncture in the related Coastal Water Project matter (A.04-09-019). Parties have worked diligently in that proceeding and a proposed settlement agreement was filed and served in A.04-09-019 on April 7, 2010. As stated in the Amended Scoping Memo, it is important to recognize the unique role that the Local Agencies play in endorsing the Regional Project.

A brief review of these inter-related proceedings will provide the necessary context here. As the Commission noted in D.09-12-017:

This proceeding is a successor proceeding to Application (A.) 97-03-052, which was California-American Water Company's (Cal-Am) application for a certificate of public convenience and necessity (CPCN) to construct the Carmel River Dam and Reservoir. Because of several intervening events, including legislation directing the Commission to identify a long-term water supply contingency plan to replace the diversions from the Carmel River, Decision (D.) 03-09-022 dismissed that application without prejudice and expressly

directed Cal-Am to file a new application to seek Commission authorization to pursue the Coastal Water Project.

On September 20, 2004, Cal-Am filed A.04-09-019 which, among other things, sought the issuance of a CPCN to construct and operate its proposed Coastal Water Project and also sought approval to increase rates to fund the proposed project. Because the application did not include a Proponent's Environmental Assessment (PEA), a necessary precursor to evaluating the merits of the proposed project and associated proposed rate increase, the assigned Administrative Law Judge (ALJ) suspended the procedural process for this matter until such time as the PEA was filed.

On July 14, 2005, Cal-Am filed an amended application, its PEA, and a Motion for Interim Rate Relief. Cal-Am concurrently began the Public Notice process required by Rule 24 of the Commission's Rules of Practice and Procedure (Rules). On July 29, 2005, the Division of Ratepayer Advocates (DRA) and the Monterey County Water Resources Agency (MCWRA) filed responses to the motion. On August 8, 2005, Cal-Am filed a reply to the responses, which was supplemented on August 10, 2005. On August 15, 2005, several parties filed protests to Cal-Am's amended application. On August 25, 2005, Cal-Am filed a reply to the protests.

On September 6, 2005, the assigned ALJ determined that there should be two distinct phases to this proceeding. Phase 1 addressed interim rate relief and the Commission has issued D.06-12-040, which authorized Cal-Am to implement the Special Request 1 Surcharge commencing January 1, 2007, to collect authorized preconstruction costs. That decision also authorized Cal-Am to implement the Special Request 2 Surcharge if the Commission issues a CPCN for the Coastal

Water Project, or alternative long-term supply solution, in Phase 2 of this proceeding.<sup>8</sup>

The Commission has also issued D.08-01-007 in A.04-09-019, which adopted a settlement between Cal-Am and DRA, whereby Cal-Am was authorized to recover \$9.31 million as compensation in full for all Coastal Water Project preconstruction costs incurred through December 31, 2006. Cal-Am filed A.08-04-019 to recover preconstruction costs incurred in 2007, and the Commission approved a settlement in D.08-12-034 that allows Cal-Am to recover \$3.74 million for those costs. Cal-Am continues to track preconstruction costs and files annual applications to request recovery of these costs. Together with the costs authorized for recovery in today's decision, Cal-Am's ratepayers have funded a total of \$18.15 million in preconstruction costs incurred through 2008. On April 1, 2010, Cal-Am filed A.10-04-004 to request recovery of an additional \$5,423,221 incurred in preconstruction costs in 2009.

In sum, the applications and decisions in A.97-03-052, A.04-09-019, A.08-04-019, and A.09-04-015 are inter-related and address several inter-related issues. As the Joint Amended Scoping Memo explained, we do not agree that the Coastal Water Project Memorandum Account can be viewed through the narrow lens that DRA recommends. Instead, we affirm the assigned Commissioner and ALJ's determination that the Commission endorsed a broader approach conceptually in D.03-09-022. For example, while the Commission noted that Cal-Am's proposed Coastal Water Project was the same as the project identified in the Plan B Project Report,<sup>9</sup> the Commission also directed Cal-Am to

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<sup>8</sup> D.09-12-017 at 2-3, footnotes omitted.

<sup>9</sup> D.03-09-022, footnote 1 at 3.

“thoroughly explore opportunities for partnerships with other regional water supply entities as it prepares its PEA and to incorporate such partnerships in the project if appropriate.”<sup>10</sup> Thus, we are not convinced that a petition to modify D.03-09-022 is required, particularly because A.04-09-019 is a successor proceeding to A.97-03-052. We note that evidentiary hearings were not held in A.97-03-052.

We conclude that, pursuant to Pub. Util. Code § 1708, the ALJ, as presiding officer, provided proper notice by serving the Amended Scoping Memo on the service list to A.97-03-052, A.04-09-019, and to the service list for this proceeding. The ALJ also provided the requisite opportunity to be heard by allowing parties to brief this issue and to file motions identifying material disputed issues on this topic that required evidentiary hearings. No party requested evidentiary hearings in A.09-04-015. Accordingly, we find that the assigned Commissioner and ALJ reasonably amended the scope of this proceeding to include issues related to the proposed Reimbursement Agreement. Further, we conclude that it is reasonable to allow Cal-Am to track the costs and revenues associated with the proposed Reimbursement Account in the Coastal Water Project Memorandum Account as of March 10, 2010, and we affirm the Joint Scoping Memo Ruling.

#### **8. Is it Reasonable to Approve the Reimbursement Agreement?**

As to the merits of the proposed Reimbursement Agreement, Cal-Am asserts that its advancement of funds to the Local Agencies is reasonable and, indeed, that such interim financing is necessary and prudent in order for Cal-Am to comply with the SWRCB’s Cease and Desist Order. Cal-Am and the Local

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<sup>10</sup> *Id.* at 12.

Agencies maintain that the costs identified in the proposed Reimbursement Agreement are directly related to the Regional Project, and, most importantly, would not have occurred but for this Project.

These parties explain that the critical project development costs that the short-term interim payment of funds would address include the design and permitting of test wells, efforts to acquire the real property interests necessary to allow construction of test wells, efforts to secure grants and least-cost financing available to Local Agencies, environmental review of the Regional Project at the federal level (pursuant to the National Environmental Policy Act, or NEPA), which is a prerequisite to receiving federal grants and funding, and efforts to secure permits for the project (should it be approved). The Local Agencies' direct project-related costs would also be covered by the Reimbursement Agreement and would include administrative project-related costs for all non-attorney staff of the agencies and legal costs for participation by "inside and outside attorneys" representing the agencies in all project-related activities, including but not limited to completion and documentation of settlement discussions and appropriate agency approval of same, environmental review required pursuant to the California Environmental Quality Act (CEQA) and project approval by each agency, and a defense of any CEQA or other legal or regulatory challenges to project approval. The Reimbursement Agreement would also cover consultant and engineering costs required for Regional Project approval and permitting.

The Local Agencies emphasize that MCWD incurred these costs at the request of DRA and this Commission, and that MCWRA became involved in order to seek a viable regional solution to the very real water constraints on the Monterey Peninsula, while at the same time ensuring compliance with its

mandate to ensure that groundwater is not exported from the Salinas Valley Groundwater Basin. The Local Agencies contend that they must participate in developing the Regional Project, both in order to ensure the viability of the Regional Project and because, in their view, there is no viable alternative. According to the Local Agencies, absent replacement of the Carmel River diversions, either Cal-Am would be subject to heavy penalties from the SWRCB or the Monterey Peninsula would be subject to extreme economic challenges. Since the Local Agencies must participate in the Regional Project, and since Cal-Am's ratepayers will consume most of the desalinated water, the Local Agencies further contend that it is reasonable for Cal-Am's ratepayers to fund the development of the Regional Project. Cal-Am and the Local Agencies emphasize that funding through the Reimbursement Agreement will not exceed \$4.3 million and that it will cover costs incurred from March 10, 2010 (the date the Joint Amended Scoping Memo allowed tracking of such costs in the Coastal Water Project Memorandum Account) until December 31, 2010 or financing is obtained for the Coastal Water Project, whichever occurs first.

DRA explains that it supports the Regional Project, subject to the concerns and conditions described in its comments and testimony in A.04-09-019, but has certain concerns regarding the proposed Reimbursement Agreement. DRA does not dispute the need for the Reimbursement Agreement as to environmental work to ensure compliance with CEQA and for NEPA, nor does DRA dispute the need for drilling of test wells; DRA acknowledges that such costs are appropriately recoverable from Cal-Am's ratepayers. Thus, DRA supports the Reimbursement Agreement for the Local Agencies' reasonable and necessary expenses, including internal and external administrative, consultant, and legal expenses associated with the Environmental Scope of Work and the Test Well

Scope of Work. However, DRA contends that funding the Local Agencies' internal and external administrative, consultant, and legal expenses associated with litigation in support of the Regional Project is very problematic. DRA asserts that such costs cannot be funded because this approach both contravenes the intervenor compensation statutes and violates the "free speech rights of ratepayers under both the United States and California Constitutions."<sup>11</sup>

DRA contends that – at least for costs associated with litigation that may ensue with regard to the Regional Project – the administrative, consultant, and legal costs that may be undertaken by the Local Agencies should be considered through the lens of the intervenor compensation statutes (Pub. Util. Code §§ 1801 et seq.). Since the statutory definition of "customer" in § 1802(b) expressly excludes any public government agency, DRA maintains that the Local Agencies' recovery of administrative, consultant, and legal costs associated with litigation is improper and not allowed by statute.

As set forth in the Joint Amended Scoping Memo, it is important that we address the proposed Reimbursement Agreement in context. Both DRA and the MPWMD oppose the proposed Settlement Agreement and Water Purchase Agreement at issue in A.04-09-019. It appears that DRA is most concerned about the Local Agencies' ability to propound what it views as burdensome and inappropriate discovery requests and to advocate for the proposed Settlement Agreement in A.04-09-019. While recognizing that utility representation before the Commission is generally considered a cost of doing business as a utility, and reimbursed in rates, DRA states that:

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<sup>11</sup> DRA Opening Brief at 7.

Representation and defense by the public utility of its own litigation positions is the standard in Commission proceedings and should be sufficient here (footnote omitted). Allowing Cal-Am to fund the Local Agencies to support its litigation positions unfairly gives Cal-Am several additional bites at the apple. To the extent that the Local Agencies' participation in A.04-09-019 is necessary to reach agreement on a Regional Project, and to provide technical details in the proceeding, the Local Agencies stand to benefit from such a Regional Project and should allocate the resources to participate at their own expense.<sup>12</sup>

DRA also argues that use of ratepayer funds to finance third-party participation in our proceedings, where such participation is "contrary to ratepayer interests," violates the free speech rights of ratepayers. DRA appears to be arguing that allowing funding for litigation costs in the Reimbursement Agreement is akin to allowing rate recovery for political lobbying or legislative advocacy, and compelling ratepayers to associate with particular forms of speech.

While DRA is correct that this Commission does not allow rate recovery for political lobbying, the Commission does allow rate recovery for litigation costs, as DRA recognizes.<sup>13</sup> Here, DRA asserts that the litigation function at issue is not really litigation, but rather is "analogous" to political lobbying or legislative advocacy.<sup>14</sup> We do not agree that the litigation function covered under the Reimbursement Agreement can be construed as political speech. To the extent that litigation costs are ultimately found to be recoverable in rates,

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<sup>12</sup> DRA Opening Brief at 6.

<sup>13</sup> See, e.g., D.09-07-038 at 5 and D.09-07-021 at 91.

<sup>14</sup> DRA Comments on Proposed Decision at 3.

these costs are a business expense and are related to the development costs of the water supply project, as Cal-Am and the Local Agencies point out.<sup>15</sup>

DRA's argument is based solely upon the fact that the Local Agencies are taking litigation positions that DRA regards as "inconsistent with Cal-Am ratepayer interests," because those positions may result in incremental costs to Cal-Am ratepayers.<sup>16</sup> DRA's contentions obviously turn on the definition of ratepayers' interests. While it is DRA's statutory mission to focus on costs and their impact on rates,<sup>17</sup> the Commission as a whole must consider the viability of the Coastal Water Project and the need for water on the Monterey Peninsula.

Indeed, we agree with Cal-Am that the approach in the proposed Reimbursement Agreement is more akin to the funding provided by Cal-Am to MPWMD in D.06-11-050 regarding joint conservation activities.<sup>18</sup> In this case, the Local Agencies have key responsibilities related to the proposed Regional Project addressed in the proposed Settlement Agreement at issue in A.04-09-019. As contemplated in the proposed Settlement Agreement, MCWRA would drill and operate the brackish source wells, MCWD would own and construct the desalination plant, and Cal-Am would own and construct the conveyance facilities needed to distribute the water to its ratepayers. We will consider that proposal in due course in A.04-09-019.

DRA's concerns regarding discovery are not compelling. While we frown on irrelevant discovery requests, there are procedures in place to address such

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<sup>15</sup> Cal-Am's Reply Brief at 8; Joint Reply Brief of MCWD and MCWRA at 9.

<sup>16</sup> DRA Comments on Proposed Decision at 3.

<sup>17</sup> Pub. Util. Code § 309.5(a).

<sup>18</sup> D.06-11-050 at 26-27.

concerns. DRA appears to arguing that the burdensome discovery issues are the consequence of MCWD and MCWRA not paying their own litigation costs; in other words, if the Local Agencies were solely responsible for their own costs, litigation and associated discovery disputes would be minimized. We do not arrive at the same conclusion.

While it is true that discovery issues before the Commission are often less contentious than those in the courts, it is certainly not unheard of for proceedings before the Commission to involve major discovery disputes.<sup>19</sup> The fact that this contentious, long-running, and complicated proceeding, dealing with multiple jurisdictions and sets of ratepayers, triggered contentious discovery does not prove anything about the proper allocation of litigation costs. Here, the parties appear to have resolved their concerns on their own – a practice we encourage. Pursuant to Rules 11.3 and 11.7, all parties may refer discovery disputes to the assigned ALJ, and they may also be referred by the ALJ to the Law and Motion Judge.

Moreover, we are not persuaded that the participation of the Local Agencies in our proceedings should be categorized as intervenor compensation activities. The Local Agencies have not put themselves forward as intervenors seeking compensation; indeed, they recognize that this is a unique proceeding with a unique set of circumstances to be considered. Our determinations in this matter are not precedential.

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<sup>19</sup> For example, D.07-07-040 referred to the voluminous pleadings and motions filed in Complaint (C.) 05-12-004 (*Chevron Products Company v. Equilon Enterprises, LLC dba Shell Oil Products US and Shell Trading (US) Company*).

At this Commission alone, parties have been arguing about the Coastal Water Project in one form or another for well over a decade. Water constraints on the Monterey Peninsula have been identified since the 1940s.<sup>20</sup> The issues involved in solving the water constraints on the Monterey Peninsula are difficult, complex, and extremely pressing. We commend DRA for initiating the discussions among community members and local entities under the auspices of the Regional Plenary Oversight Group, now known as Water for Monterey County.<sup>21</sup> The Local Agencies have now stepped forward and coordinated with Cal-Am in order to work toward development of a proposed Regional Project. We see this approach – which we may or may not ultimately approve – as a unique public-private partnership, the terms of which are under consideration in A.04-09-019. While we do not address the merits of the Regional Project here, we do wish to ensure that the Local Agencies can continue to participate throughout the proceedings at the Commission. DRA acknowledges that the Local Agencies' participation in the Regional Project is necessary, despite disputing the recovery of litigation costs.<sup>22</sup>

As demonstrated in Exhibit A to the Joint Motion, costs associated with project management and environmental documentation required under the Environmental Scope of Work are \$733,367 and costs associated with project management and test well development are \$786,300, for a total of \$1,519,667.

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<sup>20</sup> D.09-12-017 at 6 and FEIR at 2-2.

<sup>21</sup> Declaration of Steven Kasower in Support of Joint Reply Brief of Marina Coast Water District and Monterey County Water Resources Agency Regarding Reimbursement Agreement at 1-2.

<sup>22</sup> DRA Reply Brief at 7.

Joint Parties have also built in a contingency amount of \$156,830 for this work. Costs associated with administrative, consultant, and legal expenses equal \$1,600,000 for MCWD and \$1,100,000 for MCWRA.

The costs associated with agency administrative, consultant, and legal expenses through December 31, 2010 are estimated at \$2.7 million out of a total \$4.3 million, at issue here. We cannot easily distinguish the costs that are solely associated with litigation from this amount, nor can we separate the amount of agency administrative, consultant, and legal expenses that are associated with Environmental or Test Well scopes of work – amounts that DRA does not contest and, indeed, supports. We note that DRA does not dispute funding certain costs associated with litigation; for example, DRA does not appear to dispute the Reimbursement Agreement's provision to fund the Local Agencies' potential need to defend CEQA challenges in court. At this point, it makes little sense to suspend Local Agency participation in the Coastal Water Project development of a Regional Project for an amount likely to be less than \$2.7 million.

Accordingly, we will approve the Reimbursement Agreement and allow Cal-Am to advance funds to the Local Agencies on an interim basis to address cash flow concerns, with minor modifications. We expect that all funds advanced by Cal-Am will be fully repaid with interest by the Local Agencies, should the Regional Project be approved and built. To the extent that these funds are not repaid, it is reasonable for ratepayers to be responsible for funding associated with the Environmental and Test Well Development Scopes of Work, as DRA agrees. These functions are necessary to pursue the Regional Project, in any case.

At this point in the pursuit of a long-term solution to the constrained water supplies, we find that Cal-Am may advance funds for the Local Agencies to

participate in A.04-09-019. We note that ultimate recovery of legal costs is an issue in A.04-09-019. Here, we are addressing a cash flow issue.

DRA argues that there is no record evidence that the Local Agencies were subject to cash flow concerns. On the contrary, as the Joint Parties explained in their initiating motion:

Without interim assistance in the form of a Reimbursement Agreement from CAW to cover the agencies' costs between now and the date the public agencies' respective portions of an approved project can be bonded, the agencies' cash flow issues will significantly impede their full participation in the CPCN proceeding and may jeopardize their ability to participate effectively in the proceeding at all. The need is real, and a successful outcome for the Coastal Water Project proceeding may hang in the balance.<sup>23</sup>

While no documentary corroborating evidence was presented, neither was it sought. DRA had the opportunity to seek evidentiary hearings if it questioned the premise of the Joint Motion, but did not do so. The Joint Amended Scoping Memo and Ruling of the Assigned Commissioner and Administrative Law Judge stated with specificity that "[i]f parties believe that there are material disputed factual issues related to the proposed Reimbursement Agreement that require evidentiary hearings, they should file and serve a motion by May 7, 2010."<sup>24</sup> As we discussed above, no party filed such a motion.

We do clarify that the funds advanced to the Local Agencies should not provide funding for costs expected to be incurred in the normal course of business in terms of the functions covered by the Reimbursement Agreement.

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<sup>23</sup> Joint Motion at 2.

<sup>24</sup> Joint Amended Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge, issued March 10, 2010 at 8.

The Local Agencies should carefully delineate and track all functions covered by the Reimbursement Agreement and funds repaid to Cal-Am. We commend the Local Agencies for working collaboratively to ensure the success of the proposed Regional Project. While we cannot and do not assert jurisdiction over the Local Agencies, we must ensure that Cal-Am's ratepayers are protected from costs the Local Agencies would otherwise have to expend, absent this Project.

At DRA's behest, we also require that Cal-Am and the Local Agencies separately delineate and track the litigation costs included in the Reimbursement Agreement. The ultimate recovery of the litigation costs are at issue in A.04-09-019 and will be resolved in that proceeding. With these minor clarifications, we approve the proposed Reimbursement Agreement and the terms outlined in Exhibit A of the Joint Motion filed and served on February 26, 2010. The monies advanced by Cal-Am cannot exceed \$4,376,497, less any amounts for costs incurred in the normal course of business. In comments to the proposed decision, DRA correctly points out that the text of the Reimbursement Agreement states that the amounts covered shall not exceed \$4.3 million, and urges that the decision be revised accordingly. Exhibit A to the Reimbursement Agreement more precisely estimates the monthly cash flow requirements at \$4,376,497. To the extent that we have more precise estimates available, those estimates should be used. It is also reasonable to limit the Reimbursement Agreement to this amount. As these parties recognize, Cal-Am and the Local Agencies must seek additional Commission authority to extend or increase the limits set forth under the Reimbursement Agreement.

Cal-Am should carefully segregate and identify all costs subject to the Reimbursement Agreement in the Coastal Water Project Memorandum Account. Cal-Am has requested confirmation that the utility will earn interest on the

sub-account established in the Coastal Water Project Memorandum Account, which is tied to the interest rate established in D.03-09-022, currently set at the 90-day commercial paper rate. We acknowledge that Cal-Am has filed a petition to modify D.06-12-040 to request a modification to the interest rate applied to that account and such adjustments can be made prospectively, should we approve the petition for modification.

We remind Cal-Am that costs recorded in the Coastal Water Project Memorandum Account, including the Reimbursement Agreement sub-account, will be subject to review when Cal-Am seeks future approval to transfer costs from the Coastal Water Project Memorandum Account to the Special Request 1 Surcharge Balancing Account. As we noted recently in our approval of the Cease and Desist Order Memorandum Account established in Resolution W-4824:

Authorization of a memorandum account does not mean that the Commission has decided that the types of costs to be recorded in the account should be recoverable in addition to rates that have been otherwise authorized, e.g., in a general rate case. Instead, the utility shall bear the burden when it requests recovery of the recorded costs, to show that additional recovery of the types of costs recorded in the account is appropriate, that the utility acted prudently when it incurred these costs and that the level of costs is reasonable. Thus, Cal-Am is reminded that just because the Commission has authorized a memorandum account does not mean that recovery of costs in the memorandum account from ratepayers is appropriate. As such, Cal-Am will bear the burden of showing that the costs it has incurred are reasonable when seeking to amortize the balance in this account.<sup>25</sup>

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<sup>25</sup> Resolution W-4284 at 6. Similar requirements have been stated in several Commission decisions, most recently in D.10-04-030 in Conclusion of Law 6 at 22.

## **9. Comments on Proposed Decision**

Pursuant to Pub. Util. Code § 311(g)(1) and Rule 14.3, the proposed decision of the ALJ was mailed for comment on July 13, 2010. Cal-Am MCWD, and MCWRA, jointly, and DRA timely filed and served comments. DRA contends that changes to the proposed decision are required due to legal and technical concerns. We have carefully weighed the arguments set forth in the comments and modified the decision as appropriate. Cal-Am, MCWD, and MCWRA jointly filed and served reply comments.

## **10. Assignment of Proceeding**

John A. Bohn is the assigned Commissioner and Angela K. Minkin is the assigned ALJ in this proceeding.

### **Findings of Fact**

1. As detailed in the Partial Settlement Agreement, we find that Cal-Am should be allowed to recover \$5,095,213 in 2008 preconstruction costs, and this amount constitutes the entirety of Cal-Am's preconstruction costs through December 31, 2008, for which recovery has not been previously authorized.

2. \$5,095,213 should be transferred from the Coastal Water Project Memorandum Account to the Special Request 1 Surcharge Balancing Account for recovery from Cal-Am's ratepayers.

3. Nothing in the Settlement Agreement affects Cal-Am's ability to recover preconstruction costs incurred for the Coastal Water Project after December 31, 2008, and tracked in the memorandum account approved in D.03-09-022.

4. The applications and decisions in A.97-03-052, A.04-09-019, A.08-04-019, and A.09-04-015 are inter-related and address inter-related issues.

5. In D.03-09-022, the Commission directed Cal-Am to explore opportunities for partnerships with other regional water supply entities as it prepares its PEA and to incorporate such partnerships in the project if appropriate.

6. A petition to modify D.03-09-022 (in A.97-03-052) is not required in order to address the issues raised by the Joint Motion for Expedited Approval of Reimbursement Agreement, particularly because A.04-09-019 is a successor proceeding to A.97-03-052.

7. Evidentiary hearings were not held in A.97-03-052.

8. The Reimbursement Agreement is designed to address short-term interim payment of funds to the Local Agencies for the purpose of developing Test Wells, additional environmental work, and to address administrative project-related costs for all non-attorney staff of the agencies and legal costs for participation by external and internal counsel representing the agencies in project-related activities.

9. The Local Agencies have not identified themselves as intervenors seeking compensation under the Commission's intervenor compensation program, and should not be so considered.

10. As proposed in the Settlement Agreement and Water Purchase Agreement at issue in A.04-09-019, the Local Agencies have integral responsibilities related to the proposed Regional Project.

11. The issues involved in solving the water constraints on the Monterey Peninsula are long-standing, difficult, complex, and pressing.

12. In 2006, DRA initiated discussions and invited MCWD to participate in ongoing discussions and community meetings that have ultimately resulted in the proposed Regional Project.

13. Under the proposed Settlement Agreement and Water Purchase Agreement at issue in A.04-09-019, MCWRA would own and operate the brackish source water wells, MCWD would own and operate the proposed desalination plant, and Cal-Am would own and operate the conveyance and pipeline system for water distribution to its customers.

14. As demonstrated in Exhibit A to the Joint Motion filed on February 26, 2010, costs associated with project management and environmental documentation required under the Environmental Scope of Work are \$733,367 and costs associated with project management and test well development are \$786,300, for a total of \$1,519,667. Joint Parties have also built in a contingency amount of \$156,830 for this work.

15. Total costs associated with administrative, consultant, and legal expenses equal \$1,600,000 for MCWD and \$1,100,000 for MCWRA. Of these amounts, the costs associated with agency administrative, consultant, and legal expenses associated with the Environmental and Test Well Scopes of Work are not easily discernable in Exhibit A.

16. Cal-Am's ratepayers have been responsible for \$18.15 million in preconstruction costs incurred from 2006 through 2008, and ratepayers may also be responsible for an additional \$5.4 million in preconstruction costs incurred in 2009 (currently under review in A.10-04-004).

17. While the text of the Reimbursement Agreement limits the funds advanced by Cal-Am to \$4.3 million, Exhibit A to the Reimbursement Agreement establishes a more precise estimate of \$4,376,497 to address monthly cash flows through year-end.

18. The Local Agencies have agreed to repay Cal-Am the funds advanced, with interest, as of December 31, 2010, or when financing is in place for the proposed Regional Project (should it be approved), whichever event occurs first.

19. Although DRA disputes the evidentiary basis of the Local Agencies' assertion regarding cash flow concerns, DRA had the opportunity to seek evidentiary hearings and did not do so.

### **Conclusions of Law**

1. The Partial Settlement Agreement between Cal-Am and DRA is reasonable in light of the whole record, consistent with the law, and in the public interest and should be approved.

2. Pursuant to Pub. Util. Code § 1708, the ALJ, as presiding officer, provided proper notice of the amended scope of this proceeding by serving the Amended Scoping Memo on the service list to A.97-03-052, A.04-09-019, and to the service list for this proceeding.

3. Parties were provided with the requisite opportunity to be heard because parties were allowed to brief the issues related to the proposed Reimbursement Agreement and to file motions identifying material disputed issues on this topic that required evidentiary hearings. No party requested evidentiary hearings in A.09-04-015.

4. It is reasonable to affirm the expanded scope of this proceeding and to allow Cal-Am to track the costs and revenues associated with the proposed Reimbursement Account in the Coastal Water Project Memorandum Account as of March 10, 2010, and we affirm the Joint Amended Scoping Memo and Ruling issued on the same date.

5. Pub. Util. Code §§ 1801 et seq. (the statutes governing the Commission's intervenor compensation program) are not applicable to the Local Agencies and

their participation in developing the proposed Regional Project or in seeking funds advanced by Cal-Am in order to address cash flow concerns.

6. Costs incurred by the Local Agencies for litigation at this Commission or in other forums cannot be construed as political speech; to the extent that such costs are ultimately found to be recoverable, these costs are business expenses related to the development of an urgently-needed water supply project.

7. It is reasonable to approve the Reimbursement Agreement amounts as to the undisputed costs associated with the Environmental and Test Well Scopes of Work.

8. At this point, it is reasonable to allow Cal-Am to advance funds to the Local Agencies to allow their continued participation in A.04-09-019.

9. It is reasonable to require the Cal-Am and the Local Agencies to carefully delineate and track the litigation costs at issue in this proceeding, so that recovery of these costs can be considered in A.04-09-019.

10. It is reasonable to approve the more precise estimate of \$4,376,497 in monthly cash flows presented in Exhibit A to the Reimbursement Agreement, but to limit the Reimbursement Agreement to that projected amount.

11. Costs recorded in the Coastal Water Project Memorandum Account, including the Reimbursement Agreement sub-account, will be subject to review when Cal-Am seeks future approval to transfer costs from the memorandum account to the Special Request 1 Surcharge Balancing Account.

12. The Reimbursement Agreement sub-account should be subject to the same interest rate established for the Coastal Water Project Memorandum Account in D.03-09-022, currently set at the 90-day commercial paper rate.

13. The Reimbursement Agreement we approve today is a unique situation, and should not be considered precedential in any way.

14. This decision should be effective today so that the Partial Settlement Agreement and the modified Reimbursement Agreement may be implemented expeditiously.

15. A.09-04-015 should be closed.

## **O R D E R**

Therefore, **IT IS ORDERED** that:

1. The Partial Settlement Agreement between California-American Water Company and the Division of Ratepayer Advocates is approved without modification.

2. California-American Water Company is authorized to transfer \$5,095,213 of costs incurred for the Coastal Water Project through December 31, 2008 from the Coastal Water Project Memorandum Account to the Special Request 1 Surcharge Balancing Account.

3. The Joint Motion of California-American Water Company, Marina Coast Water District, and Monterey County Water Resources Agency for Expedited Approval of Reimbursement Agreement is granted, subject to the following clarifications:

- a. The terms described in the Reimbursement Agreement regarding funds advanced to Marina Coast Water District and to Monterey County Water Resources Agency to address the Environmental Scope of Work outlined in Exhibit B of the Joint Motion are approved;
- b. The terms described in the Reimbursement Agreement regarding funds advanced to Marina Coast Water District and to Monterey County Water Resources Agency to address Test Well Scope of Work outlined in Exhibit B of the Joint Motion are approved;

- c. The terms described in the Reimbursement Agreement regarding funds advanced to Marina Coast Water District and to Monterey County Water Resources Agency to address the Scope of Work outlined in Exhibit B of the Joint Motion as to Administrative, Consultant, and Legal functions are approved, to the extent the funds cover direct costs of functions required for the Environmental Scope of Work and the Test Well Scope of Work;
- d. California-American Water Company may advance funds to Marina Coast Water District and Monterey County Water Resources Agency to address the legal functions associated with addressing Application 04-09-019 at the California Public Utilities Commission or in other forums. Such costs shall be delineated and tracked by Marina Coast Water District and Monterey County Water Resources Agency in presenting their invoices to Cal-Am for reimbursement, and Cal-Am shall track these costs separately in its Reimbursement Agreement sub-account;
- e. As set forth in Exhibit A to the Reimbursement Agreement, the funds advanced to Marina Coast Water District and Monterey County Resources Agency shall not exceed \$4,376,497, less adjustments for costs that would be incurred in the normal course of business; and
- f. California-American Water Company, Marina Coast Water District, and Monterey County Water Resources Agency must seek additional Commission authority to extend or increase the funding limits set forth in the Reimbursement Agreement.

4. Application 09-04-015 is closed.

This order is effective today.

Dated August 12, 2010, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
DIAN M. GRUENEICH  
JOHN A. BOHN  
TIMOTHY ALAN SIMON  
NANCY E. RYAN  
Commissioners