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.

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

OPENING BRIEF OF THE OFFICE OF RATEPAYER ADVOCATES

SUZIE ROSE
Senior Utilities Engineer
Office of Ratepayers Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-1254
E-mail: Suzie.Rose@cpuc.ca.gov

VANESSA YOUNG
Attorney for the
Office of Ratepayers Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-3942
E-mail: Vanessa.Young@cpuc.ca.gov

December 15, 2017
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>TABLE OF AUTHORITIES</td>
<td>ii</td>
</tr>
<tr>
<td>SUMMARY OF RECOMMENDATIONS</td>
<td>1</td>
</tr>
<tr>
<td>I. INTRODUCTION</td>
<td>1</td>
</tr>
<tr>
<td>II. PRESENT AND FUTURE PUBLIC CONVENIENCE AND NECESSITY OF THE PROJECT</td>
<td>2</td>
</tr>
<tr>
<td>A. Reasonableness of Projection of Demand and Proposed Plant Size</td>
<td>3</td>
</tr>
<tr>
<td>1. Estimates and Analysis of Demand</td>
<td>3</td>
</tr>
<tr>
<td>2. Estimates and Analysis of Supply Alternatives</td>
<td>7</td>
</tr>
<tr>
<td>3. Need for and Appropriateness of Proposed Plant and Plant Size</td>
<td>9</td>
</tr>
<tr>
<td>B. Cost and Financing</td>
<td>12</td>
</tr>
<tr>
<td>1. Reasonableness of Proposed Cost Cap</td>
<td>12</td>
</tr>
<tr>
<td>2. Financing Issues</td>
<td>16</td>
</tr>
<tr>
<td>3. Apportionment of Risk in the Event Production is Insufficient in</td>
<td>18</td>
</tr>
<tr>
<td>Whole or in Part of a Significant Plant Component during the</td>
<td></td>
</tr>
<tr>
<td>Operating Life of the MPWSP</td>
<td></td>
</tr>
<tr>
<td>C. Feasibility and Desirability of Using Solar and Renewables</td>
<td>19</td>
</tr>
<tr>
<td>D. Section 1002 Factors</td>
<td>20</td>
</tr>
<tr>
<td>III. LEGAL PRINCIPLES IN SUPPORT OF AND IN OPPOSITION OF MPWSP</td>
<td>20</td>
</tr>
<tr>
<td>A. Site restrictions</td>
<td>20</td>
</tr>
<tr>
<td>B. Agency Act</td>
<td>20</td>
</tr>
<tr>
<td>IV. SETTLEMENTS</td>
<td>20</td>
</tr>
<tr>
<td>V. OTHER</td>
<td>21</td>
</tr>
<tr>
<td>VI. CONCLUSION</td>
<td>21</td>
</tr>
</tbody>
</table>
# TABLE OF AUTHORITIES

## CPUC DECISIONS

<table>
<thead>
<tr>
<th>Decision</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Decision 83</td>
<td>10, 18, 24</td>
</tr>
<tr>
<td>D.10-12-016</td>
<td>10</td>
</tr>
<tr>
<td>D.12-10-030</td>
<td>10</td>
</tr>
<tr>
<td>D.13-07-048</td>
<td>10</td>
</tr>
<tr>
<td>D.14-05-001</td>
<td>10, 11</td>
</tr>
<tr>
<td>D.16-09-021</td>
<td>17</td>
</tr>
</tbody>
</table>
SUMMARY OF RECOMMENDATIONS

If the Commission authorizes a certificate of public convenience and necessity for the Monterey Peninsula Water Supply Project (MPWSP, including a desalination plant, the risk of success or failure of a water supply solution (or solutions) must be borne entirely by Cal Am’s shareholders. If Cal Am fails to successfully manage the risks related to the MPWSP, the costs associated with these failures should not be borne by Cal Am’s ratepayers. The Commission must build ratepayer protections into any decision issued in this proceeding to 1) ensure that these risks are not transferred to Cal Am’s ratepayers, and 2) encourage Cal Am to make reasonable and prudent management decisions.

Specifically, if the Commission decides to authorize a CPCN for the MPWSP, it is crucial that the authorizing decision provides for ratepayer protections and considerations, including but not limited to the following:

1. A detailed after-the-fact reasonableness review of the final costs and of the actual utility of the MPWSP facilities should be conducted before any amounts are added to the ratebase for the Monterey District. The reasonableness review should include an assessment of the extent to which the facilities are used and useful, as well as the extent to which the facilities are producing water for Cal Am’s ratepayers.

2. If Cal Am fails to successfully manage construction and implementation of the desalination plant, any additional costs related to this failure should not be borne by ratepayers.

3. Ratepayers should not be responsible for any additional costs related to risks that rightfully belong with the utility, such as: a) The return water percentage required, b) Avoidable construction cost overruns, c) Costs related to legal action regarding the groundwater basin, d) High operations and maintenance costs, operational issues, or other circumstances resulting in an abandoned Plant.

4. Regardless of what size desalination plant may be authorized as a maximum plant size by the Commission, Cal Am should bear the responsibility of utilizing sound judgement in determining the appropriate sized facility to construct. Accordingly, the Commission should ensure that:
a) If Cal Am constructs a desalination plant that is larger than that which the system demand justifies, the costs associated with constructing the additional plant capacity should not be borne by ratepayers.

b) If Cal Am is utilizing the desalination plant at its maximum capacity, yet not utilizing other available sources of supply such as purchased water from Pure Water Monterey, Carmel River water (to the extent allowable), and aquifer storage and recovery (to the extent available), then the desalination plant should only be considered “used and useful” to the extent that it is not supplanting other available sources of supply.

5. Cal Am’s request to increase the cost cap for the MPWSP above the amount agreed to in the Comprehensive Settlement Agreement should be rejected, as Cal Am has not satisfied its burden of proof that the increase is reasonable and prudent, and the existing cost caps in the Comprehensive Settlement Agreement are a material part of an agreement that was negotiated as a whole.

6. Cal Am’s recommendations for modifications to Surcharge 2 result in an unreasonable and unacceptable risk to ratepayers. Approving Cal Am’s proposal significantly erodes ratepayer protections carefully considered and negotiated in the Comprehensive Settlement Agreement for Surcharge 2.

7. If the Commission decides to authorize Surcharge 2, costs should be tracked separately in a memorandum account, independent of any other surcharge or costs. Should the MPWSP not be completed, the entire amount collected under Surcharge 2 should be returned to customers.

8. If the Commission chooses to consider the possibility of additional purchased water from Pure Water Monterey as a potential alternative to authorizing construction of Cal Am’s proposed desalination facilities, the costs and benefits of this option should be further developed, studied, and considered.

9. Cal Am should be required to pursue the most cost-effective energy procurement methods consistent with California’s green-house gas (GHG) reduction goals. It would be imprudent to require Cal Am to utilize solar on a stand-alone basis due to the inadequate examination of cost differentials and operational implications of renewable energy sources.
The Commission has long held that “The Public Utilities Act is no magic talisman insuring public utilities against failure in case good judgment is not exercised in the financing and construction thereof.”¹ If Cal Am fails to successfully manage the risks associated with the MPWSP, any increase in costs associated with this failure should not be borne by Monterey District ratepayers.

¹ Decision 83, p.9.
OPENING BRIEF OF THE OFFICE OF RATEPAYER ADVOCATES

I. INTRODUCTION


In July 2013, sixteen parties, including ORA jointly filed a Settlement Agreement (Comprehensive Settlement Agreement) regarding issues related to the groundwater replenishment project (Pure Water Monterey, formerly GWR), the hydrogeologic study, the desalination plant and Cal-Am Only facilities, operations and maintenance costs, environmental factors including erosion and energy conservation, contingencies, financing of the Monterey Peninsula Water Supply Project (MPWSP), ratemaking, and corporate governance. Also, in July 2013, eight parties, including ORA, jointly filed a

Settlement Agreement on Plant Size and Operation. These settlement agreements are still pending before the Commission.

II. PRESENT AND FUTURE PUBLIC CONVENIENCE AND NECESSITY OF THE PROJECT

Pursuant to Public Utilities Code (PU Code) § 100, a Certificate of Public Convenience and Necessity (CPCN) requires the applicant to demonstrate that “present or future public convenience and necessity require or will require such construction.” In addition, California-American Water Company (Cal Am) has the duty to uphold other statutory obligations including PU Code § 8201 which provides: “Any water company having a franchise to use the streets of a city, shall properly and adequately serve with water the inhabitants of the territory for the service of which it has such franchise. As used in this section, to ‘properly and adequately serve with water’ includes furnishing water of a quality meeting or exceeding standards established by the State Department of Health pursuant to Section 4026 of the Health and Safety Code.” Also, PU Code § 451 requires that “Every public utility shall furnish and maintain such adequate, efficient, just, and reasonable service, instrumentalities, equipment, and facilities … as are necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.”

In this instance, before issuing a CPCN, the Commission must determine whether Cal Am has met its burden of establishing that present and/or future public convenience and necessity requires or will require the construction of a desalination plant in Cal Am’s Monterey District. The Commission must also consider whether there is sufficient evidence in the record that Cal Am will continue to properly and adequately provide water service to its Monterey District consistent with PU Code § 8201. If a CPCN is authorized, Cal Am must continue to maintain adequate, efficient, just, and reasonable service that is necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.”

---

Monterey customers and the public at-large. Consistent with these statutory requirements, the Commission must consider whether the Monterey Peninsula Water Supply Project, which proposes construction of a desalination plant, is a reasonable and fair solution to the water constraints in the Monterey Peninsula that will satisfy the Cease and Desist Order provisions mandated by the State Water Resources Control Board while providing protection for Cal Am ratepayers in Monterey.

A. Reasonableness of Projection of Demand and Proposed Plant Size

1. Estimates and Analysis of Demand

Future water demand estimates by the parties range from 9,698 acre feet per year (AFY) to 14,355 AFY. The factors in greatest dispute among the parties related to demand estimates are the calculation of existing demand, the permanency of the drought conservation measures, and the extent of growth in the Monterey District related to legal lots of record, Pebble Beach demand, and economic recovery of the hospitality industry. Ultimately, there is significant uncertainty as to future demand, and the estimates of future demand vary widely among the parties.

a) Future Use by Existing Customers

A number of parties have called into question the reasonableness of Cal Am’s future demand forecast. The differences of opinion relate to the permanency of reductions in demand that occurred during drought restrictions, and whether demand will rebound post-drought. To estimate future demand, Mr. Crooks, on behalf of Cal Am, took the average of two methods. The first method took three averages, 1) the 10-year average demand from 2007 through 2016, 2) the average demand from 2010 through 2014, and 3) the highest 10-year (2012-2021) maximum month demand. The second method incorporates assumptions from Cal Am’s Urban Water Management Plan regarding projected post-drought bounceback in gallons per capita daily (gpcd) use, and

---

4 State Water Resources Control Board Order WR 2009-0060.
5 CA-51, Crooks Direct, p.10, Lines 14-27.
projected population growth.\textsuperscript{6} Utilizing this method, Cal Am postulates that demand would reach 12,971 AFY sometime between 2021 and 2025.\textsuperscript{2} Cal Am estimates the normalized\textsuperscript{8} annual system demand by taking the average of these two methods, arriving at an estimated demand of approximately 12,350 AFY, excluding demand for lots of record, Pebble Beach build-out, and economic recovery.\textsuperscript{9}

Cal Am contends that the drought restrictions are “not wholly permanent” and that once drought restrictions are lifted, customer demand will rebound, so in turn, drought restriction reductions should be added to future projected demand based on historic actual usage.\textsuperscript{10} The Monterey Peninsula Regional Water Authority agrees that existing demand is “likely to rise to some extent during normal years.”\textsuperscript{11}

The City of Marina asserts that conservation measures may not be so temporary where various statewide policies continue to require limits on water consumption, and contends that the increase in customer demand projected by Cal Am is not consistent with these policies, and therefore not realistic.\textsuperscript{12} The City of Marina contends that the future demand that Cal Am projects is not based on the “‘new normal’ of California water conservation” but rather on pre-drought circumstances.\textsuperscript{13}

The Monterey Peninsula Water Management District (Water Management District) similarly puts forward that the state conservation policy measures are intended as the new way of life for Californians and that the rebound cannot be “soundly predicted, nor is it likely” in light of the more permanent water use reduction programs

\textsuperscript{6} \textit{Id} at 11-13.
\textsuperscript{2} CA-51, Crooks Direct, p.13.
\textsuperscript{8} Mr. Crooks defined “normalized” as conditions where drought restrictions and CDO restrictions are present. (EH Transcript, p.3963, Lines 15-26.)
\textsuperscript{9} CA-51, Crooks Direct, p.13.
\textsuperscript{10} CA-55, Stephenson Rebuttal, p. 6, Lines 3-4; Transcript, p. 4309, Lines 21-24.
\textsuperscript{11} RWA-27, Kampe, p.6, Lines 23-24.
\textsuperscript{12} MNA-2, City of Marina, House Direct, pp.6-9.
\textsuperscript{13} MNA-2, City of Marina, House Direct, p.12, Lines 4-6.
implemented by the Water Management District.\textsuperscript{14} The Water Management District also provides a critique of Cal Am’s estimation techniques, rightfully pointing out (among other issues) that Cal Am’s “Method 2” (which is utilized in its calculation of estimated future demand) reflects future population growth, thereby resulting in double-counting when Cal Am adds legal lots of record onto this amount.\textsuperscript{15} The Water Management District states that instead, existing demand should be first calculated, and then increases in that demand added on incrementally.\textsuperscript{16} Marina Coast Water District attests to customers preserving their drought consumption habits post-drought where state-wide conservation policies continue to remain in place and where customers will be more cognizant to avoid waste and over-consumption in this post-drought period.\textsuperscript{17}

According to the Monterey Peninsula Water Management District, Monterey District’s water consumption demand has been driven down by not only drought restrictions but also other factors such as the general rate increase in effect as of late 2013.\textsuperscript{18} The Water Management District brings this to light in its testimony, and Cal Am later mentions this as a cause for the decline in demand in its rebuttal testimony.\textsuperscript{19}

The City of Marina estimates future demand at around 9,300 AFY in 2021 (as opposed to the 12,350 AFY estimated by Cal Am), under the assumption that price impact and conservation policies will keep future average customer demand at approximately the same level as current average customer demand (excluding Lots of Record and Pebble Beach).\textsuperscript{20} Surfrider Foundation and the Planning and Conservation League estimate that by Year 15 after a new water supply is online, customer demand

\begin{footnotes}
\textsuperscript{14} WD-15, Stoldt, p.9, Lines 2-12.
\textsuperscript{15} Id at 10.
\textsuperscript{16} Id.
\textsuperscript{17} MCD-36, Marina Coast Water District, Van der Maaten, p.3, Lines 21-26; p.8, Lines 26-28.
\textsuperscript{18} WD-15, Stoldt, p.8, Lines 14-17.
\textsuperscript{19} CA-55, Stephenson Rebuttal, p.6, Lines 11-18; Transcript, p.4310, Lines 13-17.
\textsuperscript{20} MNA-2, City of Marina, House, p.12.
\end{footnotes}
will increase around 300 AFY from current demand, to an estimated 9,698 AFY. The Monterey Peninsula Water Management District believes 10,400 AFY is a reasonable estimate of future use by existing customers, based on the most recent 5-yr average demand (excluding 2017). In consideration of the lower demand levels during drought years along with the averages for the 5-year (2010 through 2014) and 8-year periods (2007 through 2014), the Monterey Peninsula Regional Water Authority estimated that future demand of 12,000 AFY was reasonable.

b) Growth (legal lots of record, Pebble Beach, and economic recovery of hospitality industry)

Cal Am’s future demand calculation includes its previous estimates (from 2013) for legal lots of record, Pebble Beach demand, and the economic recovery of the hospitality industry (“tourism bounceback”). Some parties argue that there is no anticipated rebound in tourism and, in turn, no addition to the current demand estimate is required. The City of Marina claims that Cal Am’s lots of record estimate is not supported by evidence in the record and should be reduced to reflect a more reasonable forecast. The Monterey Peninsula Water Management District continues to support 1,181 AFY as a reasonable estimate for legal lots of record but recommends a decrease in Pebble Beach demand and tourism bounce back figures originally proposed by Cal Am. Parties’ projections for customer demand, including lots of record, Pebble Beach, and tourism bounceback, are summarized in the table below.

---

21 SF-2, Minton, pp. 5-7. (Mr. Minton’s “current demand” estimate is based on the average of the past 36 months of demand. The 300 afy estimate is based on data from the Monterey Peninsula Water Management District)

22 WD-15, Stoldt, p.10, Line 15, p.15, Table 2.


24 CA-51, Crooks, p.7 Tables 1 and 1am.

25 MNA-2, City of Marina, House, p.10, Lines 13-16; Marina Coast Water District, Van Der Maaten, p.5, Lines 8-11; Minton, p.8.

26 MNA-2, City of Marina, House, p.10, Lines 2-11; Marina Coast Water District, Van Der Maaten, p.4, Lines 25-27 and p.5, Lines 1-6.

27 WD-15, Stoldt, pp.13-14
2. Estimates and Analysis of Supply Alternatives

Cal Am’s estimates of supply from the Carmel River, Seaside Basin, Aquifer Storage and Recovery (ASR), the Sand City Desalination Plant, and Pure Water Monterey (formerly GWR) have remained the same as in 2013 and are not disputed by the City of Marina, Surfrider Foundation, the Planning and Conservation League, the Monterey Peninsula Regional Water Authority, or the Monterey Peninsula Water Management District.\(^{35}\)

With supply estimates generally not in dispute, it is the variability in demand estimates that drives the parties to take contrasting positions with regard to supply.

---

\(^{28}\) CA-51, Crooks, p. 14, Table 4.

\(^{29}\) SF-12, Minton, p.6, Table 2.

\(^{30}\) MNA-2, House, p. 14, Table 3.


\(^{32}\) WD-15, Stoldt, Table 2.

\(^{33}\) RWA-27, Kampe, pp. 6-7.

\(^{34}\) Mr. Stoldt included estimates for Non-Revenue Water and Salinas Valley Return Flows. For purposes of comparison, these amounts were excluded from this total.

\(^{35}\) WD-15, Stoldt, p.16, Table 3; MNA-2, House, p.14, Table 3; SF-12, Minton, p.6, Table 2; RWA-27, Kampe, pp.6-8.
alternatives. In Cal Am’s 2017 testimony, Cal Am’s updates demand estimates in relation to supply and asserts that a desalination plant sized at 6.4 million gallons per day (mgd) is appropriate to meet demand.\textsuperscript{36} In contrast, when taking into consideration the City of Marina’s “corrected” water demand projection for 2021, customer demand is largely met through existing supply and therefore, there is no need for the desalination plant that Cal Am proposes.\textsuperscript{37} Surfrider Foundation and the Planning and Conservation League support a downsized desalination plant, however state that other available supplies are equally important to consider given the relatively small shortfall between supply and demand based in its calculations.\textsuperscript{38}

a) \textbf{Potential Expansion of Pure Water Monterey (amounts and costs of available water)}

Most parties support a diverse water supply portfolio\textsuperscript{39} consisting of the desalination plant, Pure Water Monterey and ASR in addition to Cal Am’s existing sources of the Carmel River and the Seaside Basin to serve the needs of the customers of the Monterey District. Monterey Regional Water Pollution Control Agency (MRWPCA) proposes three scenarios to expand Pure Water Monterey to produce additional water for Cal Am to purchase. MRWPCA’s proposal to expand Pure Water Monterey to 5 mgd and beyond is still a consideration and has not been authorized by the MRWPCA.\textsuperscript{40} These scenarios, just now being contemplated, are likely several years away from being authorized and constructed. There is still uncertainty surrounding CEQA, financing, long-term source water availability, and the ability to obtain permits for the expanded Pure Water Monterey project. Therefore a significant amount of uncertainty exists as to what the purchased water cost would be for Cal Am. Because of this uncertainty, there is not yet enough information available to fully assess the costs and benefits to Cal Am.

\textsuperscript{36} CA-51, Crooks, p.15, Lines 14-16.
\textsuperscript{37} MNA-2, City of Marina, House, p.13, Lines 12-17.
\textsuperscript{38} SF-12, Minton, p. 11.
\textsuperscript{39} Comprehensive Settlement Agreement dated July 31, 2013, p.4.
\textsuperscript{40} PCA-7, Sciuto Direct, p.2, Lines 21-23.
customers of purchasing additional water from an expanded Pure Water Monterey project.

If MRWPCA was able to expand Pure Water Monterey, and Cal Am were able to purchase enough water from this project that the construction of a desalination facility was not necessary, it could be significantly cheaper for Cal Am customers. However, pursuit of purchasing water from an expanded Pure Water Monterey project as the sole means of addressing the necessary reductions in Carmel River diversions would also remove one of the proposed supplies from the water supply portfolio approach that Cal Am initially proposed, and many parties initially supported. 41

Overall, there is still a significant amount of uncertainty regarding the potential expansion of the Pure Water Monterey project, as well as uncertainty regarding the costs and benefits of Cal Am purchasing additional water from an expanded Pure Water Monterey project. If the Commission chooses to consider the possibility of additional purchased water from Pure Water Monterey as a potential alternative to authorizing construction of Cal Am’s proposed desalination facilities, the costs and benefits of this option should be further developed, studied, and considered – including the effects of reducing the amount of supply sources in the proposed water supply portfolio.

b) Availability of water for purchase, including from Marina Coast Water District

ORA has no comment with regard to this issue.

3. Need for and Appropriateness of Proposed Plant and Plant Size

This Commission has found there is an urgent need to find an alternative water supply to replace Cal Am’s water supplies that are drawn unlawfully from the Carmel River. 42 Cal Am’s Monterey District is served by scarce water resources and has a continuing water supply deficit. 43 Most of the Monterey District's current water demand

---

41 Comprehensive Settlement Agreement dated July 31, 2013, p.4.
42 Decision (D.)10-12-016, pp. 27 and 55.
is met by water diverted from the Carmel River without a water right. Cal Am's prior applications for water supply replacement solutions have all intended to achieve a state-mandated shift away from large-scale dependence on the Carmel River but all have failed to come to fruition thus far. This instant application, filed in 2012, seeks the Commission’s approval of the Monterey Peninsula Water Supply Project. The MPWSP sets forth a portfolio of solutions intended to solve the Monterey District’s current and long-term water supply needs. Cal Am remains subject to a Cease and Desist Order issued by the State Water Resources Control Board requiring Cal Am to cease all illegal diversions by December 31, 2021 and implementing project milestones including the issuance of a CPCN for the MPWSP by September 30, 2018 and the commencement of construction September 30, 2019.44

In its very first volume of published decisions, the Commission wanted it “clearly understood” in all future applications for CPCNs that “People who finance public utilities in this State must continue to take the risk of success of the venture just as they have always done in the past.”45 If the Commission grants a CPCN for the MPWSP and Cal Am successfully manages the risks associated with the venture, Cal Am will be rewarded with a return on a significantly increased ratebase for the Monterey District, funded by Monterey ratepayers.46 If Cal Am fails to successfully manage its risks, Cal Am should not be allowed to collect such costs from ratepayers.47 “Ratepayers deserve fairness and certainty.”48 The Commission has previously authorized the construction of water treatment plant that was later found to be incapable of treating water at the maximum capacity stated in the utility’s application.49 In that case, the Commission declared that both the overrun costs and the recovery of costs at the maximum cap authorized for the

45 Decision 83, Railroad Commission of California, May 30, 1912, p.9 (as cited in DRA-20, Rose Testimony, p. 12, Lines 5-6).
46 DRA-20, Rose Testimony, p. 12, Lines 21-23.
47 DRA-20, Rose Testimony, p. 12, Lines 21-23.
48 D.14-05-001, p. 22.
49 D.14-05-001, p. 25.
project were “not remotely reasonable” given the little production that resulted from the project. If a CPCN for the MPWSC is granted, whether for a 6.4 mgd or another sized plant, the Commission should ensure that if Cal Am fails to successfully manage construction and implementation of the desalination plant, that failure should not be borne by ratepayers.

Similarly, if a CPCN is granted authorizing construction of a desalination plant, regardless of what size is authorized as a maximum plant size, it is Cal Am’s responsibility to utilize sound judgement in determining the appropriate size facility to construct. If Cal Am constructs a desalination plant that is larger than which the system demand justifies, the costs associated with constructing the additional plant capacity should not be borne by ratepayers. Additionally, in anticipation of considering at some future time whether the desalination plant is “used and useful,” it is important to note that Cal Am has multiple water supply options – therefore “used” would not necessarily equate with “useful.” If Cal Am is utilizing the desalination plant at its maximum capacity, yet not utilizing other available sources of supply such as purchased water from Pure Water Monterey, Carmel River water (to the extent allowable), and ASR (to the extent available), then the desalination plant should only be considered “used and useful” to the extent that it is not supplanting other available sources of supply.

The Commission must build protections for ratepayers, such as those discussed above, into any CPCN that may be issued in this proceeding.

a) Potential Methods of Reduction from Proposed Size

(1) Postponement of one or more wells
(2) Operation of plant at lower rate
(3) Construction of Modular Increments
(4) Other

50 D.14-05-001, p. 20 and p. 22.
51 DRA-20, Rose Testimony, p. 12, Lines 24-26.
ORA has no specific comments relating to this section.

B. Cost and Financing

1. Reasonableness of Proposed Cost Cap

The Commission should reject Cal Am’s request to increase the cost cap for the MPWSP from the amount agreed to in the Comprehensive Settlement Agreement.\(^{52}\) Cal Am has not satisfied its burden of proof that the increase is reasonable and prudent.

PU Code section 1005.5 requires that a CPCN that authorizes new construction specify the “maximum cost determined to be reasonable and prudent for the facility.”\(^{53}\) Section 1005.5 further provides that after construction and after the project is deemed used and useful, the Commission then considers whether the actual costs are reasonable and prudent and within the maximum cost specified by the Commission in the CPCN.\(^{54}\)

The Comprehensive Settlement Agreement that resulted from lengthy and intensive negotiations included cost caps related to the 6.4 and 9.6 MGD plants, as well as cost caps related to the Cal Am Only Facilities. The Comprehensive Settlement Agreement provides combined cost caps for the 6.4 MGD desalination plant and Cal Am Only Facilities as $295.66M, and for the 9.6 MGD desalination plant and Cal Am Only Facilities as $338.40M.\(^{55}\) As detailed in the Comprehensive Settlement Agreement, above these amounts, a Tier 2 Advice Letter would be necessary. Combined amounts above which a petition for modification would be necessary (as detailed in the Comprehensive Settlement Agreement) are $330.38M for the 6.4 MGD desalination plant and $384.68M for the 9.6 MGD desalination plant.\(^{56}\)

In Cal Am’s 2017 testimony, Cal Am requests an approximate 11.3% increase in the cost caps negotiated in the Comprehensive Settlement Agreement for the MPWSP, while at the same time indicating that the project will deliver approximately 22.5% less


\(^{53}\) See PU Code section 1005.5(a).

\(^{54}\) See PU Code section 1005.5(d).


\(^{56}\) Id.
water to ratepayers than initially anticipated.\textsuperscript{57} Both of these changes are cause for concern.

**Increase to Cost Caps**

As further discussed below, Cal Am does not satisfy its burden of proof in establishing that the proposed larger cost caps as presented in its 2017 testimony are reasonable and prudent. The record does not include any direct evidence supporting the updated cost estimates proposed by Cal Am in its post-2013 testimony. Moreover, there is little to no basis for the escalation rate that Cal Am uses. This is cause for concern because a significant portion of the increase in Cal Am’s cost estimates in its post-2013 testimony is due to this escalation rate.

While Cal Am’s 2017 testimony provides an Attachment with tables showing its updated cost estimates,\textsuperscript{58} Cal Am has not included in the record any workpapers or substantiation for the amounts listed in its tables. Cal Am also did not include in the record any workpapers or substantiation for the amounts listed in the cost update tables submitted post-2013 (for all cost updates submitted after parties negotiated the Comprehensive Settlement Agreement).

It appears that a significant portion of the increase in Cal Am’s cost estimate is due to the escalation of its pre-2013 cost estimates. In its 2017 cost updates, as well as in previous cost updates, Cal Am utilizes an escalation allowance of 3.5\% per year for the desalination plant and 2\% for all other project components, except the ASR System.\textsuperscript{59} However, Cal Am does not provide any justification for utilizing these amounts beyond simply stating that the numbers are based on the Engineering News-Record (ENR) escalation percentages utilized at the time of the 2015 testimony update.\textsuperscript{60} Moreover, the percentages that Cal Am utilized for escalation have not been updated since 2015,\textsuperscript{61} and

\textsuperscript{57} CA-48, Cook, Appendix1, p.4-9.
\textsuperscript{58} CA-48, Cook (Errata), Appendix 1, p.3.
\textsuperscript{59} EH Transcript Volume 25, p.4525.
\textsuperscript{60} Id.
\textsuperscript{61} Id.
even in 2015 testimony, the amounts were not substantiated by any workpapers or other documentation showing the actual ENR escalation percentages. A variety of reputable sources, including the RS Means Construction Cost Index, the Bureau of Labor Statistics Consumer Price Index, and ORA’s Estimates of Non-labor and Wage Escalation Rates (which utilizes the IHS Global Insight U.S. Economic Outlook) all show significantly lower escalation rates for the years in question.\textsuperscript{62}

It is additionally important to note that the cost caps provided in the Comprehensive Settlement Agreement were negotiated in the context of the entire agreement, which included give and take on the part of all parties (as further discussed in Section IV of this brief). While previous cost updates showed increased costs, Cal Am did not recommend an increase to the negotiated cost caps until it filed its 2017 testimony. The cost caps are a substantive and fundamental part of the Comprehensive Settlement Agreement, and should be treated as such.

Cal Am has not satisfied its burden of proof that cost increases above the cost caps negotiated in the Comprehensive Settlement Agreement are reasonable and prudent. The cost caps are a substantive part of the Comprehensive Settlement Agreement. The record does not include any direct evidence supporting the updated cost estimates proposed by Cal Am in its post-2013 testimony. Moreover, there is little to no basis for the escalation rate that Cal Am uses. This is cause for concern because a significant portion of the increase in Cal Am’s cost estimates in its post-2013 testimony are due to this escalation rate. For these reasons, the Commission should reject Cal Am’s recommendation to increase the cost caps for the MPWSP.

Decrease to Estimated Water Delivered to Customers

While the cost estimates have increased, the amount of water Cal Am projects it will deliver to customers if a 6.4 MGD desalination plant is constructed has decreased by 22.5% from 2013 estimates.\textsuperscript{63} This 22.5% decrease in the estimated amount of water

\textsuperscript{62} DRA-21, DRA-22, DRA-23.

\textsuperscript{63} DRA-20, Rose Testimony, p. 5-7.
delivered to customers is due to: 1) increased estimates for return water percentages, which were updated based on the test well performance, and 2) decreased estimates for plant utilization, presumably due to decreased demand estimates.\textsuperscript{64} These estimates are Cal Am’s own estimates, utilizing Cal Am’s projections of future demand and Cal Am’s current estimates for the amount of freshwater in the desalination plant feedwater (the water coming from the proposed slant wells).\textsuperscript{65} If Cal Am’s 2017 testimony overstates customer demand, and future demand is less than projected by Cal Am, the amount of water delivered to ratepayers would further decrease from Cal Am’s current estimates, without a significant reduction in cost.

Similarly, as Cal Am states in Mr. Crooks’ rebuttal testimony “the estimated source water return obligation provided in my testimony was just that, an estimate. The actual return obligation could be, and probably will be, lower or higher than this estimate.”\textsuperscript{66} If Cal Am’s 2017 estimates understate the return water obligation, and the actual return water obligation is higher than currently estimated, this could decrease the amount of water available to Cal Am customers compared to Cal Am’s current estimates, also without a significant reduction in cost.

The testimony related to project costs and the amount of water Cal Am anticipates delivering to its customers should be scrutinized as the Commission considers whether to issue a CPCN. If the Commission decides to issue a CPCN for the MPWSP, the associated maximum cost in the authorizing decision should represent a reasonable and prudent cost for the project, based on current estimates. Additionally, it is crucial that any decision authorizing construction of MPWSP facilities require further, more detailed scrutiny of the actual amounts spent after the project is complete and before the amounts go into ratebase in order to determine the amounts that are reasonable and prudent. Additionally, before these amounts go into ratebase, it will be important to assess the

\textsuperscript{64}Id.

\textsuperscript{65}See DRA-20, Rose Testimony, at p.5-7 and Attachment 1 for a more detailed description of the changes in Cal Am’s estimates from 2012/13 testimony to 2017 testimony, as well as details of ORA’s calculation of the percentage decrease.

\textsuperscript{66}CA-52, Rebuttal Testimony of Ian Crooks, p.18.
extent to which the facilities are used and useful, as well as the extent to which the facilities are producing water for use by Cal Am’s ratepayers (as opposed to producing water to meet the return water obligation). It is imperative that any Commission decision issued allow for a detailed after-the-fact reasonableness review of the final costs and of the actual utility of the facilities before any amounts are added to the Monterey District’s ratebase. This reasonableness review should include an assessment of the extent to which the facilities are used and useful, as well as the extent to which the facilities are producing water for use by Cal Am’s ratepayers.

2. **Financing Issues**

Cal Am’s recommendations for modifications to Surcharge 2 result in an unreasonable and unacceptable risk to ratepayers. Approving Cal Am’s proposal significantly erodes ratepayer protections carefully considered and negotiated in the Comprehensive Settlement Agreement for Surcharge 2, as discussed in more detail below. If the Commission does decide to authorize Surcharge 2, Cal Am should be required to separately track costs in memorandum account, independent of any other surcharge or costs. Should the MPWSP not be completed, Cal Am should be required to return the entire amount collected under Surcharge 2 to customers.

Surcharge 2 would allow Cal Am to collect funds from customers for project costs in advance of the completion of the desalination project. The Comprehensive Settlement Agreement provides provisions for the collection and use of approximately $71.5M in Surcharge 2 funds, with the specification that the first $35M collected under Surcharge 2 would be applied to spending on the Cal Am Only Facilities.\(^\text{67}\) At the time this provision was negotiated, it provided an important ratepayer protection as discussed further below.

However, in D.16-09-021, against ORA’s recommendation, the Commission authorized $50.3 million for the Monterey Pipeline and Pump Station, two components of

\(^{\text{67}}\) Comprehensive Settlement Agreement, p.12.
the Cal Am Only Facilities.\textsuperscript{68} Therefore, as discussed in Linam’s 2017 testimony, this clause of the Comprehensive Settlement Agreement – that provides some ratepayer protection for the usage of Surcharge 2 funds – now requires modification for the agreement to be practically implementable.\textsuperscript{69} Cal Am’s recommendations for modifying this portion of the Comprehensive Settlement Agreement are to reduce Surcharge 2 from the $71.5 million in the Comprehensive Settlement Agreement to $40.0 million,\textsuperscript{70} and to “update Section 12.2 of 21 the Comprehensive [Large] Settlement to apply the first 50% of the funds collected under the MPWSP Construction Funding Charge to the ‘Remaining CAW-Only Facilities.’ The remaining 50% would be applied to the desalination plant after permits required to commence construction have been obtained.”\textsuperscript{71}

Cal Am’s recommendations for modifications of Surcharge 2 result in an unreasonable and unacceptable risk to ratepayers. The Monterey Pipeline and Pump Station have some amount of independent utility in the absence of a desalination plant, as these two facilities serve the ASR project and the Pure Water Monterey project. Funding these facilities with the first 50% of Surcharge 2 funds provides an important ratepayer protection, because in the event that the desalination plant is not built, the first 50% of ratepayer funds collected under Surcharge 2 are guaranteed to be spent on facilities that still have the potential to be used and useful. In this regard, the Comprehensive Settlement Agreement was considered with such ratepayer protections in mind.

Under Cal-Am's new proposal to collect and spend Surcharge 2 funds, the facilities that would be funded by the first 50% of Surcharge 2 funds, the “remaining Cal Am Only facilities”, do not have independent utility in the absence of the desalination plant.\textsuperscript{72} Because these facilities do not have independent utility outside of the

\textsuperscript{68} D.16-09-021 approved a memorandum account to track the costs and AFUDC for the Monterey Pipeline and Pump Station, net of any grants. Cal Am may file a Tier 2 advice letter to recover reasonable costs once these facilities are used and useful.

\textsuperscript{69} CA-53, Direct Testimony of Jeffrey Linam (Errata), p.12-13.

\textsuperscript{70} Id. at 12.

\textsuperscript{71} Id. at 14-15.

\textsuperscript{72} See generally A.12-04-019 and D.16-09-021
desalination plant, they carry the same risk as building the desalination plant itself. Approving Cal Am’s proposal significantly erodes a ratepayer protection carefully considered and negotiated in the Comprehensive Settlement Agreement.

If the Commission does decide to authorize Surcharge 2, costs should be tracked separately in a memorandum account (not netted against costs or other sources of financing), independent of any other surcharge or costs. Should the MPWSP not be completed, the entire amount collected under Surcharge 2 should be returned to customers. If the MPWSP is completed, then, as always, Cal Am bears the burden of demonstrating that all amounts spent are reasonable and prudent. The Commission should ensure that all costs covered by the amounts collected by Surcharge 2 are reviewed for reasonableness and prudency. While this should always be the case for funds spent, it is a particularly important ratepayer protection for funds collected in advance of project completion, as would be the case for Surcharge 2.

3. **Apportionment of Risk in the Event Production is Insufficient in Whole or in Part of a Significant Plant Component during the Operating Life of the MPWSP.**

As stated above, the Commission clearly established from its very first volume of published decisions that “People who finance public utilities in this State must continue to take the risk of success of the venture.” This fundamental understanding, which has guided utility regulation in California for more than one-hundred years, should serve as a compass for all apportionment of risk in Cal Am’s proposed venture in the instant proceeding.

As such, the Commission must take appropriate measures to ensure that no portion of the risk of Cal Am’s proposed venture is transferred from the utility, where it rightfully belongs, to Cal Am’s ratepayers. In the event that production is insufficient in whole or

---

24 DRA-20, Rose Testimony, p. 12, lines 12-14.
in part of a significant plant component during the operating life of the MPWSP, Cal Am shareholders should be wholly responsible for any associated costs.

Additional risks that rightfully belong with the utility include, but are not limited to:

1) The return water percentage required
2) Avoidable construction cost overruns
3) Costs related to legal action regarding the groundwater basin
4) High operational and maintenance (O&M) costs, operational issues, other circumstances resulting in an abandoned Plant.  

If the Commission grants a CPCN for the MPWSP and Cal Am successfully manages these and other risks, Cal Am will be rewarded with a return on a significantly increased ratebase for the Monterey region, funded by Monterey District ratepayers. If Cal Am fails to successfully manage these risks, any increase in costs associated with this failure should not be borne by the ratepayers. The Commission must build such protections into any decision authorizing a CPCN for the MPWSP.

C. Feasibility and Desirability of Using Solar and Renewables

Because there is an inadequate examination of cost differentials and operational implications of renewable energy sources within the evidentiary record of this proceeding, it would be imprudent to require Cal Am to utilize these technologies on a stand-alone basis. However, if a CPCN is granted, Cal Am should be required to pursue the most cost-effective energy procurement methods that ultimately contribute to the State’s green-house gas (GHG) reduction goals. As with any other project cost ultimately sought to be recovered in rates at the time a project is used and useful in providing

---

75 DRA-20, Rose Testimony, p. 12, lines 14-20.
76 DRA-20, Rose Testimony, p. 12, lines 20-23.
77 DRA-20, Rose Testimony, p. 12, lines 23-26.
78 DRA-20, Rose Testimony, p. 12, lines 26-27.
service, Cal Am, and not the ratepayers, should bear the risk of unreasonable or imprudently incurred costs.

D. Section 1002 Factors
ORA has no comment with regard to these factors.

III. LEGAL PRINCIPLES IN SUPPORT OF AND IN OPPOSITION OF MPWSP

A. Site restrictions
ORA has no comment with regard to this issue.

B. Agency Act
ORA has no comment on the legal principles associated with this issue. However, in addition to the legal principles, the Commission should thoroughly consider the costs related to complying with the Agency Act. These costs are currently uncertain, due to the uncertain amount of return water required for the desalination plant. Cal Am shareholders, and not Cal Am ratepayers, should bear the risks of increased cost and/or decreased supply due to return water percentages higher than initially anticipated.

IV. SETTLEMENTS
As discussed in Ms. Rose’s written and oral testimony, there are challenges associated with implementing the Settlement Agreements as they are currently written. While Cal Am suggests that the Comprehensive Settlement Agreement only requires “minor modifications,” any modifications to a settlement that the parties have already reached resolution on should be viewed in light of the entire agreement as a whole and all of its provisions. Here, the Comprehensive Settlement Agreement considered a variety of components including issues related to the GWR, the desalination plant and Cal-Am-Only facilities, construction costs, operations and maintenance costs, environmental factors, contingencies, financing of the MPSWP, and ratemaking. Negotiations involved

---

79 DRA-20, Rose Testimony, p. 11 and EH Volume 27, p. 4939 - 4942.
give and take among the parties. For this reason, the “minor modifications” Cal Am proposes could potentially undermine key terms negotiated by the parties that in fact enabled the parties to reach an agreement.

In reality, the changes proposed by Cal Am in its testimony are not simply minor modifications, but instead represent substantial and fundamental changes to the Comprehensive Settlement Agreement that significantly shift risks on to Monterey District’s ratepayers and away from Cal Am. One of the “minor modifications” Cal Am proposes is changing the cost caps in the Comprehensive Settlement Agreement; another is changing project financing in relation to Surcharge 2. Changing ratepayer protections built into the settlement agreements such as the cost caps and financing details of Surcharge 2 are not “minor modifications,” but in fact substantive and material changes to an agreement that is intended to be taken as a whole. The concept of modifying the cost caps in the Comprehensive Settlement Agreement is particularly concerning in light of the issues discussed above regarding: 1) unsubstantiated increases to the cost estimates (compared to previous estimates and to the cost caps in the Comprehensive Settlement Agreement), 2) decreased estimated water delivered to Cal Am customers (compared to estimates at the time the Comprehensive Settlement Agreement was negotiated), and 3) the erosion of ratepayer protections in regards to Surcharge 2 (compared to the terms of the Comprehensive Settlement Agreement).

ORA continues to express its willingness to participate in further negotiations of the terms of the settlement agreement in light of D.16-09-021.

V. OTHER

ORA has no comment with regard to this section.

VI. CONCLUSION

If the Commission authorizes a CPCN for the MPSWP, including a desalination plant, the risk of success or failure of a water supply solution (or solutions) must be borne entirely by Cal Am’s shareholders. If Cal Am fails to successfully manage the risks related to the MPWSP, the costs associated with these failures should not be borne by Cal Am’s ratepayers. The Commission must build ratepayer protections into any decision
issued in this proceeding to 1) ensure that these risks are not transferred to Cal Am’s ratepayers, and 2) encourage Cal Am to make reasonable and prudent management decisions.

Specifically, if the Commission decides to authorize a CPCN for the MPWSP, it is crucial that the authorizing decision provides for ratepayer protections and considerations, including but not limited to the following:

10. A detailed after-the-fact reasonableness review of the final costs and of the actual utility of the MPWSP facilities should be conducted before any amounts are added to the ratebase for the Monterey District. The reasonableness review should include an assessment of the extent to which the facilities are used and useful, as well as the extent to which the facilities are producing water for Cal Am’s ratepayers.

11. If Cal Am fails to successfully manage construction and implementation of the desalination plant, any additional costs related to this failure should not be borne by ratepayers.

12. Ratepayers should not be responsible for any additional costs related to risks that rightfully belong with the utility, such as: a) The return water percentage required, b) Avoidable construction cost overruns, c) Costs related to legal action regarding the groundwater basin, d) High O&M costs, operational issues, or other circumstances resulting in an abandoned Plant.

13. Regardless of what size desalination plant may be authorized as a maximum plant size by the Commission, Cal Am should bear the responsibility of utilizing sound judgement in determining the appropriate sized facility to construct. Accordingly, the Commission should ensure that:

   a) If Cal Am constructs a desalination plant that is larger than that which the system demand justifies, the costs associated with constructing the additional plant capacity should not be borne by ratepayers.

   b) If Cal Am is utilizing the desalination plant at its maximum capacity, yet not utilizing other available sources of supply such as purchased water from Pure Water Monterey, Carmel River water (to the extent allowable), and ASR (to the extent available), then the desalination plant should only be considered “used and
useful” to the extent that it is not supplanting other available sources of supply.

14. Cal Am’s request to increase the cost cap for the MPWSP above the amount agreed to in the Comprehensive Settlement Agreement should be rejected, as Cal Am has not satisfied its burden of proof that the increase is reasonable and prudent, and the existing cost caps in the Comprehensive Settlement Agreement are a material part of an agreement that was negotiated as a whole.

15. Cal Am’s recommendations for modifications to Surcharge 2 result in an unreasonable and unacceptable risk to ratepayers. Approving Cal Am’s proposal significantly erodes ratepayer protections carefully considered and negotiated in the Comprehensive Settlement Agreement for Surcharge 2.

16. If the Commission decides to authorize Surcharge 2, costs should be tracked separately in a memorandum account, independent of any other surcharge or costs. Should the MPWSP not be completed, the entire amount collected under Surcharge 2 should be returned to customers.

17. If the Commission chooses to consider the possibility of additional purchased water from Pure Water Monterey as a potential alternative to authorizing construction of Cal Am’s proposed desalination facilities, the costs and benefits of this option should be further developed, studied, and considered.

18. Cal Am should be required to pursue the most cost-effective energy procurement methods consistent with California’s green-house gas (GHG) reduction goals. It would be imprudent to require Cal Am to utilize solar on a stand-alone basis due to the inadequate examination of cost differentials and operational implications of renewable energy sources.

The Commission has long held that “The Public Utilities Act is no magic talisman insuring public utilities against failure in case good judgment is not exercised in the financing and construction thereof.” If Cal Am fails to successfully manage the risks associated with the MPWSP, any increase in costs associated with this failure should not be borne by Monterey District ratepayers.

81 Decision 83, p.9.
Respectfully submitted,

/s/ VANESSA YOUNG

Vanessa Young
Attorney
for the Office of Ratepayer Advocates

California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-3942

December 15, 2017
E-mail: Vanessa.Young@cpuc.ca.gov