

Decision 12-07-008 July 12, 2012

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of California-American Water Company (U210W) for a Certificate of Public Convenience and Necessity to Construct and Operate its Coastal Water Project to Resolve the Long-Term Water Supply Deficit in its Monterey District and to Recover All Present and Future Costs in Connection Therewith in Rates.

Application 04-09-019
(Filed September 20, 2004;
amended July 14, 2005)

**DECISION GRANTING MOTION TO WITHDRAW PETITION
TO MODIFY DECISION 10-12-016 AND CLOSING PROCEEDING**

1. Summary

By this decision, we resolve pending motions and close the proceeding in California-American Water Company's (Cal-Am) Application (A.) 04-09-019. Cal-Am notified parties on January 28, 2012, after months of mediation with the Marina Coast Water District (MCWD) and the Monterey County Water Resources Agency (MCWRA), of its conclusion that continued pursuit of the Regional Desalination Project approved by Decision (D.) 10-12-016 was not reasonable and that alternative desalination projects were under consideration. On April 23, 2012, Cal-Am filed both a withdrawal of its petition for clarification of D.10-12-016 and a new application, A.12-04-019, for approval of the Monterey Peninsula Water Supply Project. The Commission is treating the withdrawal as a motion to withdraw, and granting it.

Until now, A.04-09-019 has remained open to consider rate base offsets for Cal-Am only facilities and a Phase 3, related to cost allocation and rate design. By this decision, those matters will be considered instead in a separate proceeding. The Commission is treating the new application, A.12-04-019, as a replacement for the previous one, A.04-09-019.¹ Cal-Am is instructed to file a separate application to deal with disputed and undisputed costs, and associated cost recovery, relative to A.04-09-019. However, the Division of Water and Audits should continue processing all currently unprocessed Advice Letters dealing with rate base offsets for Cal-Am only facilities discussed in D.10-12-016. Cal-Am should not claim any costs incurred after January 17, 2012, the date Cal-Am announced its withdrawal from the Regional Desalination Project. In due course the Commission will consider any modifications that may be advisable in D.10-12-016 to have it conform with the decision here.

2. Background

California-American Water Company (Cal-Am) applied for a Certificate of Public Convenience and Necessity (CPCN) in order to provide a solution to the long-standing constraints on water supply on the Monterey Peninsula. This effort is known as the Coastal Water Project. Cal-Am is under order from the

¹ MCWD is requesting that we determine that “project cessation,” within the meaning of the Water Purchase Agreement (WPA), has occurred with regards to the Regional Desalination Project. Under the WPA (e.g., subsection 7.4), project cessation is a condition triggering certain rights and duties between Cal-Am, MCWD and MCWRA. We refrain from making a finding of “project cessation” here because the jurisdiction to resolve claims or causes of action under the WPA appears to lie with the judiciary rather than the Commission. What we do find is that Cal-Am has withdrawn its support of and role in the Regional Desalination Project; and, further, we consider A.12-04-019 a replacement for A.04-09-019.

State Water Resources Control Board to cease diverting water to which it has no legal rights, determined in 1995 to be 10,730 acre feet of water per year from the Carmel River. The utility must also replace 2,975 acre feet of water per year in allocations from the Seaside Basin.²

The Commission certified the Final Environmental Impact Report for the Coastal Water Project and various alternative projects in Decision (D.) 09-12-017. The Commission considered Cal-Am's request for a CPCN and a proposed Settlement Agreement regarding a joint proposal by Cal-Am, the Marina Coast Water District (MCWD), the Monterey County Water Resources Agency (MCWRA), the Monterey Regional Water Pollution Control Agency, Surfrider Foundation, the Public Trust Alliance, and Citizens for Public Water³ to construct, operate, and maintain a regional desalination plant, source wells, and distribution facilities. The Commission approved the Settlement Agreement and issued a CPCN to Cal-Am for the Regional Project in D.10-12-016.⁴

² The State Water Resources Control Board issued Order WR 95-10 in 1995 and Order 2009-0060 in 2009 (Cease and Desist Order). The latter order requires Cal-Am to undertake additional measures to reduce its diversions from the Carmel River and to terminate all such diversions no later than December 31, 2016. In 2006, the Monterey County Superior Court issued a final decision regarding adjudication of water rights of various parties who use groundwater from the Seaside Basin (*California American Water v. City of Seaside et al.* Case No. 66343).

³ By letter dated July 25, 2011, Citizens for Public Water informed parties to the Settlement Agreement that Citizens for Public Water rescinded its support for the Regional Desalination Project. This letter was appropriately lodged in the Correspondence File by the assigned Administrative Law Judge (ALJ).

⁴ We also approved D.11-09-036, which modified D.06-12-040 by: 1) setting the Special Request Surcharge at 15% rather than 10%; and 2) setting 4.00% as the carrying costs for the Coastal Water Project Memorandum Account.

On October 14, 2011, Cal-Am filed a Petition for Clarification and Modification of D.10-12-016 (Petition to Modify), stating that because certain impediments had occurred, it was possible that the Regional Desalination Project could be delayed or replaced with a different project. Cal-Am requested that the Commission confirm that the Cal-Am only facilities could still be built and that the costs could still be recovered, regardless of the ultimate outcome of the Regional Desalination Project. Cal-Am contended that, with the exception of the transfer pipeline, the facilities approved in D.10-12-016 that were to be built by Cal-Am would still be necessary and should be designated as used and useful for ratemaking purposes.

The assigned Commissioner and ALJ issued an Amended Joint Scoping Memo Ruling on October 27, 2011. The Division of Ratepayer Advocates (DRA) and MCWD filed responses on November 14, 2011. With permission of the assigned ALJ, Cal-Am and MCWD filed replies to the responses on November 28, 2011. The ALJ issued a Ruling on December 14, 2011 convening a prehearing conference (PHC) on January 24, 2012 to discuss the Petition to Modify and to consider the timing for Phase 3 (cost allocation and rate design) as discussed in the Joint Amended Scoping Memo Ruling. On January 18, 2012, Cal-Am filed a compliance filing to provide an update to the mediation efforts of Cal-Am, MCWD, and the MCWRA. MCWD filed a PHC statement on January 23, 2012.

At the request of the ALJ, Cal-Am filed a compliance filing and status report on March 1, 2012. MCWD and MCWRA filed separate status reports. On March 15, 2012, Cal-Am and MCWD filed responses to each party's status report. MCWRA also filed a response to both status reports. On March 20, 2012, Public Trust Alliance moved to request leave to file a late response to the status reports

which was granted by the assigned ALJ. On February 13, 2012, Water Plus filed a notice of intent to claim intervenor compensation which is denied below due to the closing of this proceeding. On April 2, 2012, LandWatch Monterey moved for party status and for leave to file a notice of intent to claim intervenor compensation. That combined motion is denied below for the same reason. On April 23, 2012, Coalition of Peninsula Businesses moved for party status and that motion also is denied below due to the closing of the proceeding.

3. Overview of D.10-12-016

In D.10-12-016, we approved a Settlement Agreement that set forth a public-private partnership among Cal-Am, MCWD, and MCWRA known as the Regional Desalination Project. As part of the Settlement Agreement, we granted a CPCN to Cal-Am for its participation in the Project, and approved without modification the Water Purchase Agreement associated with the Regional Desalination Project. As we stated in D.10-12-016:

As proposed by the Settling Parties, Monterey County Water Resources Agency would own, construct, operate, and maintain the source water wells and raw water conveyance facilities to the desalination plant. Marina Coast Water District would own, construct, operate, and maintain the desalination plant and the product water conveyance facilities to the delivery point, which then becomes Cal-Am's intake point. Cal-Am would own, construct, operate, and maintain the pipeline, conveyance, and pumping facilities necessary to deliver the water to its customers. The Monterey Regional Water Pollution Control Authority would own, operate, and maintain the outfall for return of the brine to the sea.

In approving the modified Settlement Agreement and Water Purchase Agreement, we approve Cal-Am's participation in the Settlement Agreement and issue a CPCN to Cal-Am for the following components of the Regional Project: the transfer pipeline, the Seaside pipeline, the Monterey pipeline,

including the Valley Greens pump station, the Terminal Reservoirs, and the Aquifer Storage and Recovery facilities.

With the decision we adopt today, this Commission takes the highly unusual step of finding, after thorough review, that conditioned upon full compliance with the terms and conditions of the agreements and with the current law and practice which constrains the local agencies, there are sufficient procedural, contractual, and other legal safeguards contained in the parties' agreement, when taken together with the legal mandates imposed on Cal-Am's partner agencies under current law, to be reasonably certain to produce the lowest cost, viable, and timely solution to Cal-Am's immediate source water needs so as to provide adequate water for Cal-Am's ratepayers.

In so doing we are guided by the good faith engineering estimates provided by the parties, the committed willingness of the parties to work together according to the terms of the agreements to achieve the plan as outlined, and the results of extensive public vetting of the severity of the water problem and the widespread public support of the proposed solution. We recognize that even under the best case scenario, the revenue requirement for Cal-Am's Monterey District customers would increase by approximately 63%, as compared to the projected trend of the current revenue requirement (footnote omitted). Cost allocation and rate design related to the Coastal Water Project will be addressed in Phase 3 of this proceeding and will be coordinated with Cal-Am's current General Rate Case proceeding, Application (A.) 10-07-007.

We do not make this decision lightly but only after extensive review of the information supplied by the parties over many months, extensive discussion, and a thorough analysis of the agreements, the circumstances surrounding those agreements, vigorous public vetting, a review of the applicable law, and an assessment of the political and economic situation surrounding this application, we recognize the pressing need

for the Regional Project, as well as the historic alignment of the goals of virtually all parties and the residents and businesses on the Monterey Peninsula to ensure that a secure supply of water is available before severe water restrictions imposed by the State Water Resource Control Board's Cease and Desist Order are fully implemented in 2016.⁵

In sum, we approved Cal-Am's participation in the Regional Desalination Project in recognition that time was of the essence to ensure that the ratepayers on the Monterey Peninsula would be supplied with adequate sources of potable water well before the onset of the provisions of the Cease and Desist Order. We recognized that permitting, testing, and project development and construction would be time-consuming and difficult. In December 2010, the Regional Desalination Project appeared to be a feasible project that could be constructed in time to meet the requirements of the Cease and Desist Order.

4. Petition to Modify Sought, Opposed and Withdrawn

In its October 2011 Petition to Modify, Cal-Am stated that "[d]ue to certain developments" the parties to the Water Purchase Agreement, i.e., Cal-Am, MCWD, and MCWRA, entered into mediation with a Commission-sponsored mediator.⁶ In that filing, Cal-Am stated that it is "seeking confirmation that it may continue with the construction of the California-American Water facilities (minus the transfer pipeline) no matter what the status of the Regional Desalination Project, (footnote omitted)."⁷

⁵ D.10-12-016 at 5-7.

⁶ Petition to Modify at 1.

⁷ *Id.* at 3.

Cal-Am stated that there could be “setbacks” associated with the Regional Desalination Project which could require modification or replacement with an alternative project.⁸ Cal-Am recognized that Commission approval would be required for any proposed modified or alternative project. In its Petition to Modify, Cal-Am stated that whether or not the Regional Desalination Project proceeds, the Cal-Am facilities approved in D.10-12-016 would be needed to more expeditiously move water between the northern and southern areas of Cal-Am’s distribution system, improve storage, and expand the aquifer storage and recovery (ASR) system. More specifically, Cal-Am contended that the Monterey Pipeline, the Seaside Pipeline, the Terminal Reservoir, the ASR Pipeline, the ASR Recirculation and Backflush Pipelines, the ASR Pump Station, and the Valley Green Pump Station would all be necessary to improve and enhance Cal-Am’s system. Although not proposing a particular path forward, Cal-Am included a range of eleven possible alternatives to the Regional Desalination Project to demonstrate that the Cal-Am facilities are necessary, no matter what project goes forward. In addition, Cal-Am maintained that the stand-alone facilities should be approved to enhance fire safety and ensure full use of the ASR system water.

DRA⁹ and MCWD¹⁰ each objected to the Petition to Modify on various

⁸ *Id.* at 6.

⁹ DRA objected to the Petition to Modify because these facilities were approved in conjunction with the Regional Desalination Project and Cal-Am would not have the authority to construct the facilities if the Regional Desalination Project did not go forward. If a new project were proposed, DRA stated that any authorized alternate water supply could require changes to the Cal-Am facilities approved in D.10-12-016. DRA thought it reasonable to consider the uncertainty surrounding the Regional Desalination Project, because former MCWRA Board Member Steve Collins was under

Footnote continued on next page

grounds and Cal-Am countered.¹¹ The dispute over the petition became moot on

indictment by the Monterey County District Attorney and investigation by the Fair Political Practices Commission for alleged violations of the Fair Political Practices Act. DRA essentially maintained that the record of this proceeding only addressed the Cal-Am facilities in conjunction with the Regional Desalination Project – not as stand-alone facilities, to be pursued no matter what ultimate water supply project was approved by the Commission. DRA stated that there were material issues of disputed fact associated with Cal-Am’s assertions, which have not been tested and are not supported. DRA acknowledges Cal-Am’s concerns regarding timing of the approval of its facilities but contends that an adequate record is required to assess its assertions and that the facilities must be considered holistically, i.e., in light of the project ultimately proposed by Cal-Am. DRA proposes informal meetings, formal workshops, and a new phase to this proceeding (with a new Scoping Memo) to address Cal-Am’s concerns. To do otherwise, DRA suggests, could result in harm to ratepayers since it is not clear how the Regional Desalination Project may ultimately be modified or replaced.

¹⁰ MCWD stated that the Petition to Modify was unnecessary and would add to the confusion and uncertainty surrounding the Regional Desalination Project. MCWD contended that to the extent that the petition sought a modification of the authority to construct the facilities approved in D.10-12-016 in order to support a proposed modification of or alternative to the Regional Desalination Project, such a proposal could not be considered in a Petition to Modify. Because Cal-Am included an attachment with eleven alternative projects that it was in the process of evaluating, MCWD contended that any such project must be the subject of an application to consider the proposed CPCN, cost, and environmental review. MCWD further contended that Cal-Am’s Petition to Modify was premature because there are no facts before the Commission to justify the consideration of any potential new project. MCWD also raised concerns related to the Water Purchase Agreement and Cal-Am’s obligation to uphold its contractual obligations, as MCWD saw them.

¹¹ Cal-Am disputed DRA’s and MCWD’s contentions that its proposed modifications had to be considered in light of any proposed change to the Regional Desalination Project. Instead, Cal-Am contended that its proposed modifications are very narrow and were required to allow Cal-Am to achieve the full promise of Monterey County’s water supplies. At that point, Cal-Am was seeking only clarification that it could proceed with the facilities approved in D.10-12-016 to forestall “the mistaken conclusion that [Cal-Am] may only progress with the [Cal-Am] facilities if the Regional Desalination Project will be implemented as approved.” Cal-Am Petition for Modification (October 14, 2011), at 6-7. Cal-Am argued that DRA’s proposal to consider the Petition to Modify in a new phase of the proceeding with a new Scoping Memo

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April 23, 2012, when Cal-Am withdrew the petition¹² in conjunction with the filing of A.12-04-019 that seeks approval of the Monterey Peninsula Water Supply Project.

5. Mediation, PHC, Status Reports and Litigation

On January 18, 2012, Cal-Am filed a Mediation Update, stating that “[Cal-Am] has determined that it is no longer reasonable to move forward with the Regional Desalination Project and has begun considering alternative desalination projects.” Cal-Am explained that it entered into mediation with MCWD and MCWRA on August 11, 2011 and that the mediation concluded on January 16, 2012 because the parties were unable to agree on many issues and challenges related to the Regional Desalination Project. Cal-Am explained that because of the looming deadline related to the water restrictions ordered in the State Water Resource Control Board’s Cease and Desist Order, it had to focus on proposing an alternative water supply project as quickly as possible. Cal-Am states that an expeditious decision on its Petition to Modify is still required, since “[w]ith the exception of the transfer pipeline, which is unique to the Regional Desalination Project, the [Cal-Am] facilities would be necessary for any of the 11 alternative projects that have been analyzed and are also essential to take full

Ruling was an attempt to expand the scope of the relief requested. Because Cal-Am meets with DRA (and the Division of Water and Audits) staff on a quarterly basis, Cal-Am contended that there were reasonable procedures in place to allow for discussion of the size, scope, and cost of the Cal-Am facilities. Cal-Am contended that further delay in consideration of its Petition to Modify would lead to increased construction costs and additional, unnecessary uncertainty. Cal-Am included letters from various stakeholders urging that the Commission approve its Petition to Modify.

¹² Cal-Am Withdrawal of its Petition for Clarification and Modification of D.10-12-016.

advantage of the [ASR] system and thereby reduce the Monterey County District’s diversions from the Carmel River during low river flow periods.”¹³

Although Cal-Am, MCWD, and MCWRA attempted to produce a joint status report, as directed by the ALJ, this proved impossible. In Cal-Am’s status report, timely filed on March 1, 2012, Cal-Am described the timeline leading up to its decision to withdraw its support for the Regional Desalination Project:

Date	Action
April 2011	Allegations regarding MCWRA Board Member Stephen Collins’ conflict of interest.
Letters dated July 7, 20, and August 22, 2011	By letter to Cal-Am and MCWD, MCWRA stated that Water Purchase Agreement was void based on conflict of interest allegations.
August 11, 2011	Coastal Commission declined to issue permit for test wells, based on conflict of interest allegations and lawsuits regarding California Environmental Quality Act (CEQA).
August 12, 2011	Cal-Am served notice of default of failure to obtain financing to MCWD and MCWRA based on §7.1(a) of the Water Purchase Agreement.
Late August 2011	Cal-Am, MCWD, MCWRA began confidential mediation with Commission-sponsored mediator.
September 28, 2011	Cal-Am served notice by letter to MCWD and MCWRA terminating the Water Purchase Agreement and related agreements.

¹³ Cal-Am’s Compliance Filing – Mediation Update at 2.

December 2011	Superior Court Judge issues intended decision re: Ag Land Trust, finding that MCWD is lead agency.
January 16, 2012	Parties were unable to reach agreement and the mediation process concluded.
January 17, 2012	Cal-Am publicly announced its decision to withdraw support of the Regional Desalination Project.

Cal-Am also raised concerns with CEQA. On April 5, 2010, Agricultural Land Trust filed suit against MCWD in Monterey County Superior Court, alleging that MCWD should have been the lead agency, rather than the Commission, that the Environmental Impact Report (EIR) was inadequate and raising certain issues related to water rights. In an intended decision issued in December 2011, the Superior Court found that MCWD should have been the lead agency. In an amended intended decision, issued in February 2012, the Court also determined that certain water rights issues were not adequately addressed in the EIR. Based on those intended decisions, Cal-Am contended that MCWD could either issue its own EIR, appeal the Court’s final decision, or vacate its resolutions approving the EIR as a responsible agency and approving action to purchase property known as the Armstrong Ranch (the intended site of the Regional Desalination Plant). Cal-Am adamantly contended that any of those actions would take a substantial amount of time – time that was not available, because of the implications of the Cease and Desist Order. Pursuant to the Cease and Desist Order, Cal-Am must replace 7,062 acre-feet of water no later than December 2016. Cal-Am stated that it would consider supporting the Regional Desalination Project only under the following conditions:

- (1) a court ruling that the Water Purchase Agreement and related agreements are valid in light of the conflict of interest allegations;

- (2) immediate funding for the Regional Desalination Project from MCWD and MCWRA;
- (3) a revised EIR from MCWD addressing the Ag Land Trust issues;
- (4) immediate issuance of test well permits;
- (5) repayment of the amounts owed to California American Water under the Reimbursement Agreement and the Credit Line Agreement;
- (6) an agreement among the three original parties to the Water Purchase Agreement (Cal-Am, MCWD, and MCWRA) to continue under the Commission-approved Water Purchase Agreement, including a determination on how the public agencies would fund their project expenditures in advance of being able to issue debt or to make modifications to a new Water Purchase Agreement that all three parties agreed to and seek approval in a timely fashion from the Commission for such modifications; and
- (7) a finding from the Commission confirming that the Regional Desalination Project is the best option to meet the State Water Resource Control Board's requirements.¹⁴

In response to the assigned ALJ's questions, Cal-Am contended that a significant water supply project is required, despite demand management efforts, aggressive leak repair, increased use of recycled water, and use of grey water for landscape irrigation.

In its separately-filed status report, MCWD disagreed with Cal-Am's conclusions and contended that the Commission had to order Cal-Am to move forward with the Regional Desalination Project. MCWD made a number of requests of the Commission, outside of the actual status of the Regional

¹⁴ Cal-Am Compliance Filing dated March 1, 2012, at 6.

Desalination Project. First, MCWD requested that the Commission order certain actions related to the Water Purchase Agreement parties' obligations. MCWD asked that we apply the statute of limitations to find that the Water Purchase Agreement and related contracts remain valid, despite any alleged violations of Government Code Section 1090 by Stephen Collins. MCWD contended that the Commission should order MCWRA to assign its interests to a party that will undertake those obligations, if MCWRA will not "perform its contractual obligations. . . or face legal action by the Commission."¹⁵ MCWD also requested that the Commission order Cal-Am, MCWD, and MCWRA to perform their contractual obligations related to the Water Purchase Agreement and the Regional Desalination Project. Second, MCWD asked that the Commission determine that "any final decision by the Monterey County Superior Court in the Ag Land Trust cases that purports to review, reverse, correct or annul the commission's final findings that it is the California Environmental Quality Act (CEQA) lead agency and that the Commission's Final Environmental Impact Report (FEIR) is adequate and in compliance with CEQA intrudes on the Commission's decisions, findings, and processes in violation of Pub. Util. Code § 1759(a) and the *Covalt* case."¹⁶ Third, MCWD asked that we reaffirm the findings in D.10-12-016 to the effect that the Regional Desalination Project is the "only viable replacement water supply project for the Monterey Peninsula, as demonstrated in its CEQA Findings of Fact for the Regional Desalination Project."¹⁷

¹⁵ Separate Status Report of MCWD, dated March 1, 2012, at 3.

¹⁶ *Id.* at 2.

¹⁷ *Id.* at 15.

MCWD also contended that Cal-Am was mistaken in its claims that financing was not obtained in a timely manner. MCWD contended that the parties discussed financing regularly and because of market conditions and the desire to obtain low-cost financing, Cal-Am agreed to recognize that its credit line would constitute the initial tranche of the financing plan. Cal-Am contended that such an interpretation was not consistent with the Water Purchase Agreement.

MCWRA recognized that there was substantial uncertainty and potential delay associated with the pending CEQA issues. MCWRA noted that because Monterey County Superior Court did not consolidate the Ag Land Trust lawsuit against MCWRA with the lawsuit against MCWD, it was unclear when these issues would be considered and that the determinations in the MCWD case may not apply to MCWRA. While disagreeing with Cal-Am regarding whether initial financing obtained under Cal-Am's line of credit was sufficient for purposes of § 7.1(a) of the Water Purchase Agreement, MCWRA did recognize that no institutional financing has been obtained.

Public Trust Alliance recommended that parties continue to pursue the Regional Desalination Project and that such an approach was consistent with the mandates of the public trust doctrine. Public Trust Alliance also recommends that a public process be put in place to try and address issues associated with ill-will and distrust.

On April 12, 2012, MCWD filed in the Court of Appeal of the Sixth Appellate District a petition for a writ of mandate against the Superior Court of Monterey County seeking the vacation of the Superior Court's February 29, 2012 order concerning an amended intended judgment in the Ag Land Trust CEQA case on the ground that it unlawfully intruded on the jurisdiction of the

Commission. On April 17, 2012, however, the Superior Court of Monterey County entered as a final judgment that amended intended judgment.

6. Filing of New Application by Cal-Am

The Monterey Peninsula Water Supply Project now sought by Cal-Am in A.12-04-019, in lieu of the Regional Desalination Project, is described in that application as follows:¹⁸

The Monterey Peninsula Water Supply Project will consist of slant intake wells, brackish water pipelines, the desalination plant, product water pipelines, brine disposal facilities, and related appurtenant facilities. Depending on the availability of water from the Groundwater Replenishment Project, the desalination plant will be sized at either 9.0 mgd or 5.4 mgd. California American Water is in the process of securing an approximately 46-acre parcel of land located just to the northwest of the MRWPCA's wastewater treatment plant as the site for the proposed desalination plant. California American Water is also working to secure permanent easements on an approximately 376-acre parcel of land located due west of its proposed desalination plant site for the slant intake wells. California American Water will be using a series of slant wells located west of the sand dunes to draw ocean water and potentially a small amount of groundwater from the ground. The slant wells will be approximately 700 to 800 feet in length and will feature several hundred feet of screen below the ocean floor and seaward of the mean high tide mark. The final layout and configuration will be based on the results of additional groundwater modeling that will be completed as part of the Commission's environmental review and as may be required by the California Coastal Commission or for final design.

¹⁸ Application of Cal-Am for Approval of the Monterey Peninsula Water Supply Project and Authorization to Recover All Present and Future Costs in Rates (filed April 23, 2012) at 7-8.

The Monterey Peninsula Water Supply Project also incorporates the California American Water-only facilities that the Commission previously approved in D.10-12-016. [Footnote omitted.] The California American Water-only facilities consist of the Transfer Pipeline, the Seaside Pipeline, the Monterey Pipeline, the Terminal Reservoir, the ASR Pipeline, the ASR Recirculation and Backflush Pipelines, the ASR Pump Station and the Valley Greens Pump Station. In a significant departure from historic operation, supply from the desalination plant portion of the Monterey Peninsula Water Supply Project will enter the California American Water distribution system at the metering station from the north through the Transfer Pipeline. The current configuration of the distribution system does not allow water to be conveyed from the north, to customers on the southern portion of the Peninsula. The California American Water-only facilities will convey water between the northern and southern portions of the Monterey County District. The source of the flow from the north to the south will be either the desalination plant portion of the Monterey Peninsula Water Supply Project, and/or the extraction of flows from the ASR system located in Seaside Basin.

The Monterey Peninsula Water Supply Project will be owned and operated by California American Water. (The Groundwater Replenishment Project will be publicly owned.) California American Water expects to utilize a design/build process for the desalination plant, and a design/bid/build process for the brackish water pipelines, the product water pipeline and the related pipelines. For the slant intake wells, the California American Water will determine whether a design/build or design/bid/build process is appropriate once the environmental review of the affected area has been completed.

This newly proposed project is represented by Cal-Am to be “a modified version of the North Marina Project” analyzed in the EIR certified in 2009 in

A.04-09-019.¹⁹

MCWD, seeking to perpetuate the Regional Desalination Project and asserting claims of right under the related Water Purchase Agreement, filed both a motion to intervene and a motion to dismiss, with supporting documents, on April 30, 2012.

7. Discussion

We are persuaded that Cal-Am must pursue a reasonable and feasible course of action to obtain a potable water supply in a timeframe that will allow Cal-Am to comply with the Cease and Desist Order. Cal-Am is obligated under various statutory frameworks to provide water to its customers. Pursuant to Pub. Util. Code § 8201, “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.” In pertinent part,

Pub. Util. Code § 451 requires “Every public utility shall furnish and maintain such adequate, efficient, just, and reasonable service, instrumentalities,

¹⁹ *Id.* at 22: “The main modifications are the locations of the intake slant wells and the desalination treatment plant. Due to these revised locations, a portion of the product water pipeline or finished water main will need to be routed on a previously un-surveyed corridor.”

equipment, and facilities . . . as are necessary to promote the safety, health, comfort, and convenience of its patrons, employees, and the public.”

It is unfortunate that Cal-Am withdrew its support for the Regional Desalination Project, but given the various events that have overtaken the decisions we reached in December 2010, we see no alternative but to move forward with the new application, A.12-04-019, seeking the Monterey Peninsula Water Supply Project. At this point, there is simply too much uncertainty associated with the Regional Desalination Project to force Cal-Am to pursue that project further. It is not reasonable to allow time to continue to elapse and costs to continue to accrue for the Regional Desalination Project, a project that, due to a significant change in circumstances since 2010, has no reasonable prospect of achieving its goals. In terms of the many requirements necessary to ensure that a reasonable water supply source is in place by December 2016, there is no time to lose, as Cal-Am has pointed out.

We decline to address here positions being taken by parties concerning rights and obligations under the Water Purchase Agreement. MCWD’s related contentions and requests will not be dealt with here. We are not inclined to address alleged or potential breaches of contracts.

This proceeding has been open since 2004. The assigned Commissioner and ALJ had anticipated that Phase 3 would be required to deal with cost allocation and rate design related to the Regional Desalination Project. Because Cal-Am has put forth a new proposal in A.12-04-019, we need not address cost allocation and rate design here. Therefore, we close this proceeding.

8. Disputed Costs

The assigned ALJ directed Cal-Am to provide an accounting of costs expended thus far on the Regional Desalination Project. Thus far, \$26,568,651

has been approved for recovery in pre-construction costs related to the Coastal Water Project. In A.11-06-030, Cal-Am is requesting approval of an additional \$5,354,229 in pre-construction costs accrued in 2010. Cal-Am is also tracking post 2010 costs which totaled \$687,167 as of January 31, 2012. These are not trivial amounts. Cal-Am has recovered \$14,426,284 from its customers through its approved Special Request I surcharge. Cal-Am is required to file separate applications to seek recovery of these costs.²⁰

The amounts described above do not include amounts lent to MCWD and MCWRA under the Water Purchase Agreement or under the Reimbursement Agreement approved in D.10-08-008. According to Cal-Am, MCWD and MCWRA owe Cal-Am \$6,244,852 and \$1,946,219, respectively. MCWD and MCWRA may dispute these amounts and do dispute the interpretation of the requirements in the Water Purchase Agreement and the Reimbursement Agreement. The parties have stated that they are meeting to discuss these issues and to determine whether they can be settled or must be litigated. We encourage the parties in their settlement discussions and can assign a neutral ALJ to assist in the mediations. To the extent that the disputed costs and associated cost recovery must be addressed by this Commission, Cal-Am should file a new application.

9. Pending Motions

On March 20, 2012, Public Trust Alliance filed a motion for leave to file its late response to the various status reports filed on March 1. Public Trust Alliance

²⁰ On March 31, 2012, the Commission's Executive Director granted Cal-Am's request for a six-month extension of time to file its application to seek recovery of pre-construction costs accrued in 2011.

has been an active party and was a signatory to the Settlement Agreement approved in D.10-12-016. It is reasonable to grant this motion and accept Public Trust Alliance's late response.

On February 13, 2012, Water Plus filed a Notice of Intent to Claim Intervenor Compensation. On February 24, 2012, Cal-Am filed its opposition to Water Plus's request. On April 2, 2012, LandWatch Monterey County filed a motion for party status, a motion for leave to file a late Notice of Intent and a Notice of Intent to Claim Intervenor Compensation. Because we are closing this proceeding and shifting the focus to A.12-04-019, we deny these motions as premature. To the extent that these parties determine that they wish to participate in A.12-04-019, they should make the appropriate filings in that new proceeding pursuant to the Commission's Rules of Practice and Procedure and the assigned ALJ's rulings.

10. Comments on Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on July 2, 2012, and reply comments were filed on July 9, 2012 by Cal-Am, MCWRA, MCWD and DRA.

In their comments, Cal-Am, Monterey County Water Resources Agency and MCWD have requested various clarifications of the following language that appears in the proposed decision at 2 and 24 (Ordering Paragraph 2):

...the Division of Water and Audits should continue processing all currently unprocessed Advice Letters dealing with rate base offsets for Cal-Am only facilities discussed in D.10-12-016. Cal-Am should not claim any costs incurred after January 17, 2012, the date Cal-Am announced its withdrawal from the Regional Desalination Project.

The purpose of that language is to protect Cal-Am ratepayers against additional expenditures on the Regional Desalination Project that was approved in D.10-12-016. Given that Cal-Am is proposing a new and different project that is the subject of their application A.12-04-019, it is not reasonable to expect Cal-Am ratepayers to pay for additional expenses related to a project that is no longer being pursued.

The Commission understands that there are costs that have been incurred in A.04-09-019 related to the Regional Desalination Project that may be recoverable in rates. We will examine the recoverability of such costs in other, more appropriate proceedings, and parties will have an opportunity to make their arguments that certain costs are or are not recoverable in rates.

The language at issue was not intended to prevent Cal-Am from incurring reasonable costs related to its current application A.12-04-019, nor does it limit any more general authorization Cal-Am received prior to the selection of the Regional Desalination Project.

Cal-Am's request that the cut-off date for incurring costs be changed from January 17, 2012 to January 18, 2012 is denied as the former date is when Cal-Am said in its application A.12-04-019, at 5, and elsewhere that it had publicly announced its withdrawal of support for the Regional Desalination Project.

MCWD's request that additional recitals of fact be added under Findings of Fact is rejected because they are either not necessary or bear upon the dispute between Cal-Am, Monterey County Water Resources Agency and MCWD over costs.

11. Assignment of Proceeding

Michael R. Peevey is the assigned Commissioner and Gary Weatherford is the assigned ALJ in this proceeding.

Findings of Fact

1. Pursuant to the State Water Resource Control Board's Cease and Desist Order, Cal-Am must cease diverting water from the Carmel River by the end of December 2016 and must replace 7,062 acre-feet of water, or face severe restrictions.

2. On October 14, 2011, Cal-Am filed a petition for clarification and modification of D.10-12-016, requesting confirmation that the Cal-Am only facilities (absent the transfer pipeline) would still be required for any project built and that such facilities should continue to be designated as used and useful for ratemaking purposes. On April 23, 2012, Cal-Am withdrew that petition, and filed a new application, mooted those requests.

3. Cal-Am has withdrawn its support for the Regional Desalination Project, approved in D.10-12-016.

4. While various strategies may be employed to replace the water, time is of the essence to ensure that a water supply is in place to avoid the restrictions associated with the State Water Resource Control Board's Cease and Desist Order.

5. On April 23, 2012, Cal-Am filed A.12-04-019 to propose how to move forward to provide sufficient water supply to comply with the State Water Resource Control Board's Cease and Desist Order and to avoid the stringent water supply reductions ordered by the Cease and Desist Order.

6. To date, we have approved \$26,568,651 for recovery of pre-construction costs related to the Coastal Water Project.

7. In A.11-06-030, Cal-Am is seeking an additional \$5,354,229 in pre-construction costs accrued in 2010.

8. Cal-Am has recovered \$14,426,284 from its customers thus far via Special Request Surcharge I.

9. There are additional costs, which may be in dispute, related to the MCWD and MCWRA, the Reimbursement Agreement approved in D.10-08-008, and the Line of Credit approved in the Water Purchase Agreement.

Conclusions of Law

1. It would not be reasonable to approve Cal-Am's Petition to Modify D.10-12-016 without fully determining how the Cal-Am facilities would relate to the project ultimately determined to replace the Regional Desalination Project; therefore, it is reasonable to accept Cal-Am's April 23, 2012 withdrawal of that petition.

2. Given the uncertainty surrounding CEQA, financing, and the ability to obtain permits for the Regional Desalination Project, it is not reasonable to force Cal-Am to pursue the Regional Desalination Project.

3. Cal-Am is obligated to furnish adequate and safe water to its customers, pursuant to various statutory mandates, including, but not limited to, Pub. Util. Code §§ 451 and 8201.

4. Because we are closing this proceeding, there is no need to consider Phase 3 of this proceeding, related to cost allocation and rate design at this time.

5. Public Trust Alliance is an active party in this proceeding, a signatory to the Settlement Agreement approved in D.10-12-016, and its motion for leave to file late response to the individual status reports should be granted.

6. Because we are closing A.04-09-019, it is reasonable to determine that pending motions not addressed herein are moot and to deny as premature any requests for determination of eligibility of intervenor compensation status.

7. To the extent that there are disputed costs related to the Reimbursement Agreement or the Line of Credit under the Water Purchase Agreement, Cal-Am should file a new application.

8. Today's decision should be made effective immediately.

O R D E R

IT IS ORDERED that:

1. California-American Water Company's April 23, 2012 withdrawal of its Petition for Clarification and Modification of Decision 10-12-016 filed on October 14, 2011, is treated as a motion and granted.

2. California-American Water Company shall file a new application to the extent that there are disputed costs related to the Reimbursement Agreement or the Line of Credit under the Water Purchase Agreement. However, the Division of Water and Audits should continue processing all currently unprocessed Advice Letters dealing with rate base offsets for California-American Water Company only facilities discussed in Decision (D.) 10-12-016. California-American Water Company should not claim any costs incurred for the California-American Water Company-only facilities after January 17, 2012, the date California-American Water Company announced its withdrawal from the Regional Desalination Project, in connection with the authorization in D.10-12-016. The recoverability of costs that have been incurred in Application (A.) 04-09-019 related to the Regional Desalination Project will be examined in other proceedings. Nothing herein is intended to prevent California-American Water Company from incurring reasonable costs related to its current application A.12-04-019, nor does it limit any more general

authorization California-American Water Company received prior to the selection of the Regional Desalination Project.

3. Public Trust Alliance's March 20, 2012, motion for leave to file a late response to the various status reports filed on March 1, 2012, is granted.

4. Water Plus's February 13, 2012, notice of intent to claim intervenor compensation is denied.

5. LandWatch Monterey's April 2, 2012, motion for party status and for leave to file a notice of intent to claim intervenor compensation is denied.

6. Coalition of Peninsula Businesses' April 23, 2012, motion for party status is denied.

7. Any pending motion or request not addressed herein is denied.

8. Application 04-09-019 is closed.

This order is effective today.

Dated July 12, 2012, at San Francisco, California.

MICHAEL R. PEEVEY

President

TIMOTHY ALAN SIMON

MICHEL PETER FLORIO

CATHERINE J.K. SANDOVAL

MARK J. FERRON

Commissioners