BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

In the Matter of the Application of California American Water Company (U 210 W) for an Order Authorizing Recovery of Costs for the Lease of the Sand City Desalination Facility and Associated Operating and Maintenance Costs.	Application 10-04-019 (Filed April 12, 2010)

REPLY COMMENTS OF THE DIVISION OF RATEPAYER ADVOCATES ON THE PROPOSED DECISION IN A.10-04-019

ALLISON BROWN
Attorney for
Division of Ratepayer Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-5462
Email: aly@cpuc.ca.gov

MAX GOMBERG
RICHARD RAUSCHMEIER
Analyst for
Division of Ratepayer Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Phone: (415) 703-2002
Email: mzx@cpuc.ca.gov

September 14, 2011

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

In the Matter of the Application of California American Water Company (U 210 W) for an Order Authorizing Recovery of Costs for the Lease of the Sand City Desalination Facility and Associated Operating and Maintenance Costs.	Application 10-04-019 (Filed April 12, 2010)

COMMENTS OF THE DIVISION OF RATEPAYER ADVOCATES ON THE PROPOSED DECISION IN A.10-04-019

I. INTRODUCTION

Pursuant to Rules 14.3(d) of the California Public Utilities Commission's ("Commission") Rules of Practice and Procedure ("Rules"), the Division of Ratepayer Advocates ("DRA") hereby files its reply comments on Administrative Law Judge ("ALJ") Bushey's Proposed Decision ("PD") in Application 10-04-019, California American Water Company's ("Cal Am") application for an order authorizing recovery of costs for the lease of the Sand City Desalination Plant ("SCDP") and associated operating and maintenance costs.

DRA supports the PD in its entirety and encourages the Commission to adopt it as written. Cal Am's comments contain inaccurate statements and misrepresentations of the law, facts, and condition of the record, and as such should be afforded no weight.

II. SUMMARY OF ISSUES

- Cal Am's comments contain multiple inaccurate statements and misleading assertions that distort the facts in the case.

- Cal Am misrepresents causality regarding growth in Sand City as fact by assuming that Sand City growth is a given when growth will not exist absent the plant because the rest of Cal Am's Monterey system is under a moratorium on new connections.

- Cal Am's claim that the SCDP was designed to reduce withdrawals on the Carmel River is not credible given that planning for the SCDP began in 2002 and the State Water Resources Control Board's ("SWRCB") Cease and Desist Order ("CDO") proceeding began in 2008.

- Consumption has dropped markedly in Cal Am's Monterey system since 2008 (witness the massive Water Revenue Adjustment Mechanism ("WRAM") balances that are the subject of another proceeding), disproving Cal Am's claim that additional reductions in consumption are infeasible.

- The prior proceeding, D.09-07-021 addressed the substantive issues; which is why the current proceeding did not have evidentiary hearings. Cal Am's claims that the PD failed to address issues is without merit.

- Cal Am, not the PD, has created the disincentive for future public-private partnerships by entering into a bad deal with Sand City.

- The Commission allowed Cal Am a second opportunity to justify this plant, allowing Cal Am the chance to improve the lease terms and prove that this investment is reasonable and prudent, but instead the company renegotiated a lease that is just as inequitable, if not worse, for ratepayers as the original lease the Commission rejected in D.09-07-021. The risk for operations and maintenance ("O&M") cost increases is disturbing especially given the extended lease term and the fact that Cal Am did not obtain the ability to raise development fees to offset the costs to current ratepayers.

II. DISCUSSION

A. Factual Misrepresentations

1. Cal Am's Assertion That The PD Leaves A 300 Acre-Foot/ Year Gap Is False.

Cal Am misinterprets the facts in this proceeding by falsely asserting that the PD leaves a 300 acre-foot/year ("AFY") gap (California American Water Company's Comments on the Proposed Decision of Administrative Law Judge Bushey, p. 2-4)[1]. The records in the prior Sand City proceeding (D.09-07-021), Cal Am's current GRC proceeding (A.10-07-007), and its WRAM Amortization proceeding (A.10-09-017) demonstrate that additional reductions in consumption and non-revenue water ("NRW") losses exceeding 300 AFY are possible.

In the prior GRC the Commission set a financial penalty/reward mechanism of $2018/acre-foot based on the standard water rate (D.09-07-021, p. 56). DRA showed that the unit cost of reducing NRW through an acoustic leak detection program was $1,646/acre foot (*Id*., at 62). It is clear that fixing leaky pipes is more cost-effective and could yield more water than the SCDP.

Cal Am cites the pending settlement in the current GRC as recognition that Cal Am has reduced lost water (p.6-7). However Cal Am neglects to mention that the pending settlement also requires Cal Am to adopt an action plan for further NRW reductions and requires Cal Am to set specific targets for NRW reductions.[2]

---

[1] All page references are to Cal Am's Comments on the PD, unless otherwise noted.

[2] A.10-07-007 Joint Motion for the Adoption of Partial Settlement Agreement Between The Division Of RatepayerAdvocates, The Natural Resources Defense Council, and California-American Water Company on Non-RevenueIssues in the General Rate Case, Exhibit A, Partial Settlement Agreement Between The Division of RatepayerAdvocates, The Natural Resources Defense Council and California-American Water Company on Non-Revenue Water Issues, filed July 28, 2011, pp. 3-4, 5-6 and 7-8, Attachments A, B.

.

In the WRAM Amortization proceeding, Cal Am has proposed a customer surcharge of 35% to recover the difference between actual sales and what was forecast in 2010, a total reduction in consumption of 2,429 acre-feet.[3] This drop is more than eight time as much as the 300 AFY provided by the SCDP. Thus, to claim that an incremental 300 AFY of consumption reductions might not be possible is misleading given the reductions seen in the past two years.

2. Cal Am's Assertions Regarding The Cost Effectiveness Of SCDP Water And Its Duty To Serve New Customers Are Not Supported By The Record

Cal Am misstates various facts and misrepresents the record by claiming that the SCDP is "very cost-effective." (p. 4-5.). Monterey County Code Section 10.72 states that it is illegal for a private company to own a desalination plant. Thus, Cal Am's argument (p. 5) that Sand City's ownership saves ratepayers money by eliminating Cal Am's rate of return is specious.

Cal Am's argument that it has a statutory duty to serve the potential new customers in Sand City is circular and not supported by the record. The new growth customers whom Cal Am claims a statutory duty to serve do not exist yet, and would not exist if not for the existence of the SCDP (p. 5). The SCDP was built to allow for customer growth, yet that same customer growth is now being used to justify the SCDP.

Cal Am's claim that the Monterey Peninsula Water Management District ("MPWMD") connection fees "will be used to fund new sources of water for CAW customers" is conjecture without basis in fact (p. 5). MPWMD is a separate entity from Cal Am and may use connection fees as it sees fit.

Cal Am claims that "The PD also ignores the fact that the marginal cost of water in Monterey is high and that the Monterey customers are facing significant increases when new sources of water come online." (p. 8). This is misleading because it only

[3] Cal Am's April 18, 2011compliance filing in A.10-09-017.

focuses on supply when, as demonstrated, the marginal cost of additional conservation and reductions in NRW are less than the per-acre foot cost of the SCDP water.

B. Legal Misrepresentations

1. Cal Am's Assertion That The PD Committed Legal Error By Ignoring Unrebutted Evidence Is Meritless And Should Be Ignored.

Cal Am claims that the PD commits legal error by ignoring unrebutted evidence. This claim has no merit. First, Cal Am entered evidence into the record that was untested via evidentiary hearings. The reason there were no evidentiary hearings was that all of the substantial issues had been litigated in the earlier proceeding. (See Commissioner Bohn Scoping Memo, September 30, 2010, p. 1 – "The existing record recently considered by the Commission in reaching D.09-07-021, Cal-Am's application, and the Division of Ratepayer Advocates' (DRA's) protest reveals no significant disputed issues of material fact.").

Second, Cal Am's amended lease is so similar to the lease considered in the prior proceeding that it was appropriate for the PD to rely on the prior decision's consideration of that lease. Cal Am's claim (p. 9) that the PD relies on circular reasoning is false because the prior decision's lease assessment is dispositive of the amended lease as well.

Third, the fact that the PD finds that Cal Am did not demonstrate that the SCDP water is the lowest reasonable cost is not equivalent to ignoring the evidence (p. 9). Cal Am disagrees with the PD's conclusions and findings regarding the evidence. This in no way indicates that the PD committed legal error or ignored evidence.

Cal Am's assertion that the PD ignores Cal Am's need for the SCDP water due to the CDO (p.10) ignores the Commission's standard that prudence is determined by an assessment of what the utility executives knew at the time decisions were made[4]. As was established in the prior decision, Cal Am entered into the original SCDP lease before the

[4] D.89-02-074, *Application of San Diego Gas & Electric Company for Authority to Increase its Rates and Charges for Electric, Gas, and Steam Service; And Related Matter.* 1089 Cal. PUC Lexis 128.

CDO was issued, and thus the CDO is not relevant to a determination of whether signing the SCDP lease was reasonable and prudent.

Cal Am's claim that the PD is not supported by its findings again ignores the substantial record developed in D.09-07-021. That record showed Cal Am was unable to justify the SCDP lease as cost-effective. Furthermore, there is a record in that proceeding that shows other approaches (leak detection) as more cost-effective than the SCDP. Cal Am was given another chance to justify the SCDP lease in this application, and was able to provide further justification in their response to the Assigned Commissioner's Scoping Ruling[5] . The PD found that Cal Am was unable to justify the SCDP lease as cost-effective. Again, the fact that Cal Am disagrees with the PD's findings and conclusions is not equivalent to the PD being unsupported.

2. Cal Am's Various Claims About The Significance Of Other CPUC And SWRCB Decisions Are Misleading And False (p.12-14)

When the CPUC conducted the Environmental Impact Report ("EIR") for the Coastal Water Project proceeding (A.04-09-019) it included the SCDP in water supply projections because the SCDP was already up and running and an EIR is required to include existing supplies as part of comprehensive environmental analysis. That the Commission included the SCDP in its EIR is completely unrelated to the reasonableness of the SCDP, and for Cal Am to claim that it based SCDP negotiation decisions on the Commission's EIR illustrates questionable decision making based upon overstating the significance of projects included in an EIR.

Furthermore, the Commission's decision approving the Regional Desalination Project (D.10-12-016) did not imply that the SCDP water was necessary to meet Monterey District needs. Cal Am is attempting to extract meaning where none exists, which is why Cal Am can only suggest that a decision implies something instead of citing to text.

---

[5] See *Cal Am Response to Assigned Commissioner's Ruling*, September 30, 2010,

Cal Am attempts to suggest that because the SWRCB looked favorably upon the SCDP in its CDO order that the Commission would be denying costs approved by another state agency. This is a fallacy. The SWRCB was looking strictly at water supply, not at cost, and did not order Cal Am to build the SCDP. Moreover, in its CDO, the SWRCB found that despite its investment in SCDP, Cal Am had not acted diligently to secure new water supply (hence the reason for the CDO). The SWRCB's actions are not germane to the Commission's reasonableness determination in this case.

3. Cal Am's Claims That The PD Exceeds The Scope Of The Proceeding By Requiring A Subsequent Application Relating To Outdoor Irrigation Is Unsupported.

Cal Am claims that the PD exceeds the scope of the proceeding by requiring a subsequent Cal Am application relating to outdoor irrigation (p.16). As was noted above, since 2008 consumption in Monterey has dropped significantly, indicating that there is still significant untapped conservation potential. Cal Am claims that the SCDP is necessary, but focuses on the supply side only. Cal Am's claim that the PD ignores prior conservation and NRW programs has no merit.

Finally, on page 17, in footnote 86, Cal Am acknowledges that it is tracking the SCDP costs in its CDO memo account. This is very troubling since Cal Am does not have authorization to track the SCDP costs in any memo account. Since the memo account was not authorized, Cal Am cannot request recovery of the SCDP costs via the CDO memo account if the Commission denies recovery in this proceeding.

III. CONCLUSION

The SCDP saga is a study in missed opportunities. When Sand City first proposed building the SCDP and having Cal Am pay for it, Cal Am missed the opportunity to assess whether it was a worthwhile investment by comparing it to other supply sources and demand-side actions. Then, when it filed its 2008 General Rate Case application, Cal Am missed the opportunity to fully justify its investment in the SCDP with sound testimony and analysis. Cal Am included the costs for the SCDP in purchased water

expense and did not submit any testimony supporting its investment. As the Commission found in D.09-07-021, "Rather than sound decision-making, the record suggests unquestioning support for this new water source, at any price, without regard to alternatives." (D.09-07-021, p. 66.)

In D.09-07-021, the Commission gave Cal Am the opportunity to undo the lease or to renegotiate a new lease on better terms. Cal Am renegotiated the lease and missed the opportunity to more equitably allocate costs, both between Cal Am and Sand City and between current ratepayers and future Sand City ratepayers whose existence owes to the water produced by the SCDP. Instead, Cal Am obtained a new lease with a longer term (31 years) that adds risk for O&M and major repair and replacement costs, and no ability to make new customers pay their fair share through connection fees.

Cal Am's Monterey ratepayers face an expensive future. Between the Regional Desalination Project (or alternative), the San Clemente Dam removal, the GRC proceedings, and the WRAM amortization proceedings, customers could face bills that double or triple over the next 5-7 years. These customers need Cal Am to make prudent investment decisions that minimize cost as much as possible. The record in D.09-07-021 and A.10-04-019 shows that the SCDP was not a prudent investment and that the lease terms are not reasonable. By approving the PD as written, the Commission will spare the approximately 40,000 Monterey ratepayers from $1.4 million per year in increased rates and make clear to Cal Am that it must do better to meet the burden of justifying its investments.

///

///

///

DRA recommends the Commission approve the PD without modification.

Respectfully submitted,

/s/ ALLISON BROWN

_____

Allison Brown
Staff Counsel

Attorney for the Division of Ratepayer Advocates
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102
Email: aly@cpuc.ca.gov
Phone: (415) 703-5462
Fax: (415) 703-2262

September 14, 2011