



EXHIBIT 9-A

Docket:	A.12-04-019
Exhibit Number	ORA - _____
Commissioner	C. Sandoval
Administrative Law Judge	G. Weatherford
ORA Witness	Susie Rose



ORA
OFFICE OF RATEPAYER ADVOCATES



REBUTTAL TESTIMONY

Application 12-04-019

San Francisco, California
March 22, 2016

TABLE OF CONTENTS

	<u>Page</u>
I. BACKGROUND	1
II. SUMMARY OF FINDINGS AND RECOMMENDATIONS.....	3
III. DISCUSSION OF FINDINGS	4
A. SUPPLEMENTAL TESTIMONY DEMONSTRATES THAT GWR HAS MET THE FIRST EIGHT FINDINGS OF THE SETTLEMENT AGREEMENT.	4
B. SUPPLEMENTAL TESTIMONY DEMONSTRATES THAT GWR COUPLED WITH A 6.4 MGD DESALINATION PLANT PROVIDES NUMEROUS POSITIVE BENEFITS IN COMPARISON TO A 9.6 MGD DESALINATION PLANT.	5
1. Positive Benefits Addressed in Parties' Testimony	6
2. Positive Benefit with Regards to Return Water Uncertainty	7
C. THE GWR PROJECT AND THE DESALINATION PROJECT CURRENTLY HAVE DIFFERING LEVELS OF CERTAINTY.	9
1. Schedule	9
2. Unexpected Issues Necessitating Changes in Design	10
3. Construction Costs	10
4. Cost Overruns.....	10
D. THERE ARE INCONSISTENCIES IN MPWMD AND CAL AM COST ANALYSES.	11
1. NPV Power Escalation	12
2. Version of Cost Model used in MPWMD Analysis.....	12
3. 6.4 MGD Capital Cost Scenarios	12
4. Debt Rate for MCWD Pipeline	14
5. Outfall Rental Costs	14
E. THE WPA WOULD NOT TRIGGER DEBT EQUIVALENCE FOR CAL AM.	15
F. COST ANALYSES SUBMITTED IN SUPPLEMENTAL TESTIMONY INDICATE THAT, COMPARED TO THE LARGE DESAL OPTION, THE GWR/SMALL DESAL OPTION WOULD LIKELY RESULT IN: 1) A SMALL FIRST YEAR REVENUE REQUIREMENT PREMIUM; AND 2) EITHER A SMALL NPV PREMIUM OR SMALL NPV BENEFIT.	15
G. THE NINTH FINDING REQUIRED BY THE SETTLEMENT AGREEMENT HAS NOT BEEN MET ABSENT A DEFINED PURCHASE PRICE OR PRICE CAP.	19
H. THE TERMS SET FORTH IN THE SETTLEMENT AGREEMENT AS PREREQUISITES FOR CAL AM ENTERING INTO A WPA FOR GWR WATER HAVE NOT YET BEEN MET, BUT COULD BE MET WITH WPA MODIFICATION.....	20

EXHIBIT 9-A

IV.	RECOMMENDATIONS.....	22
	A. REMOVAL OF THE “REASONABLE AND PRUDENT” LANGUAGE FROM THE WPA	23
	B. COST CAP ON PURCHASE PRICE MUST BE PROVIDED.....	23
V.	CONCLUSION.....	24

I. BACKGROUND

California American Water Company (“Cal Am”) filed Application (“A.”) 12-04-019 on April 23, 2012, seeking a Certificate of Public Convenience and Necessity (CPCN) for the Monterey Peninsula Water Supply Project (MPWSP), and authorization to recover all present and future costs associated with the MPWSP in rates. Sixteen parties, including ORA, jointly filed a Settlement Agreement,¹ establishing nine findings for the Commission to consider in relation to the determination on whether Cal Am should construct a 6.4 MGD Plant with Ground Water Replenishment (“GWR”) project or a 9.6 MGD Plant without GWR (collectively, “the GWR Determination”).² The Settlement Agreement is still pending before the Commission.

On September 23, 2013, the Commission issued an Amended Scoping Memo and Assigned Commissioner Ruling, bifurcating the proceeding and setting the scope of Phase 2.³ On November 17, 2015, the Administrative Law Judge (ALJ) issued a ruling that set the Phase 2 issues and schedule for evidentiary hearings to update cost estimates, provide current information concerning supply and demand, and do other things

¹ Settlement Agreement of California-American Water Company, Citizens for Public Water, City of Pacific Grove, Coalition of Peninsula Businesses, County of Monterey, Division of Ratepayer Advocates, Landwatch Monterey County, Monterey County Farm Bureau, Monterey County Water Resources Agency, Monterey Peninsula Regional Water Authority, Monterey Peninsula Water Management District, Monterey Regional Water Pollution Control Agency, Planning and Conservation League Foundation, Salinas Valley Water Coalition, Sierra Club, and Surfrider Foundation submitted on July 31, 2013.

² The Settling Parties’ Motion to Approve the Settlement Agreement dated July 31, 2013 summarizes the nine findings at p. 5 as follows: “(1) the GWR Project receives approval pursuant to a Final EIR, (2) adequate progress was made and is expected to continue for obtaining permits for the GWR Project, (3) sufficient legal certainty exists concerning long-term viability for GWR source water, (4) there is a lack of evidence showing health and water quality regulators will deny permits or approval, (5) the GWR Project is on schedule for completion, (6) the GWR Project’s design is at the required level, (7) a sufficiently detailed funding plan is in place, (8) terms to a Water Purchase Agreement (“WPA”) have been agreed to, and (9) the revenue requirement for the combination smaller plant/GWR is just and reasonable compared with the larger plant. A revenue requirement premium for the combination smaller plant/GWR may be just and reasonable if the combination affords significant benefits (including scheduling, diversification of water supply, and environmental benefits) over the larger plant.”

³ The Amended Scoping Memo and Assigned Commissioner Ruling (September 23, 2013) states at p. 5: “Phase 2 will focus on whether various findings can be made regarding the viability of the GWR Project, whether a smaller desalination plant can be authorized, and whether a Water Purchase Agreement should be approved between Cal-Am and the relevant public agencies managing the GWR Project. The scope of Phase 2 will also consider the terms of any proposed WPA and the revenue requirement of the WPA, vis-a-vis the desalination plant, including any projected debt equivalence for the WPA.”

EXHIBIT 9-A

1 necessary to complete the record for both Phases 1 and 2.⁴ With regard to the GWR
2 Determination, the Ruling states that “the nine criteria [in the settlement agreement] are
3 important elements in the consideration of the GWR” and “the Commission’s decision
4 must rest on broader principles, including what is just, reasonable, and in the public
5 interest.”⁵ The Ruling also set January 22, 2016 as the date for serving supplemental
6 testimony on demand and supply, brine discharge, return water, and updated information
7 necessary for the GWR Determination, and March 22, 2016 as the date for serving
8 concurrent rebuttal testimony on the issues addressed in supplemental testimony.⁶

9 ORA filed supplemental testimony on January 22, 2016 supporting the concept of
10 evaluating the nine findings listed in the Settlement Agreement, and providing specific
11 issues the Commission should consider in evaluating those findings. ORA stated its
12 intention to “review parties’ supplemental testimony, including updated cost estimates for
13 the two project alternatives, and submit more detailed recommendations in relation to the
14 GWR Determination in rebuttal testimony.”⁷ ORA has since reviewed parties’
15 supplemental testimony,⁸ and accordingly provides this rebuttal testimony with
16 recommendations regarding the GWR Determination.

17 Project updates filed in response to the November 17, 2015 ALJ Ruling provide
18 important detail necessary to perform an up-to-date comparison of project status and
19 costs for the GWR Determination. In regards to these cost updates, including costs
20 related to return water and brine disposal, Cal Am has agreed to cost caps in the
21 Settlement Agreement, with cost recovery subject to reasonableness review. Therefore,
22 ORA will not assess the reasonableness of these updates herein, and instead makes use of
23 these updates only as a means of evaluating the costs and uncertainties of the MPWSP in

⁴ Administrative Law Judge’s Ruling Setting Evidentiary Issues and Schedule to Complete the Record for Phases 1 and 2 (November 17, 2015) at p. 8.

⁵ Ibid. at p. 8.

⁶ Ibid. at p. 12.

⁷ Supplemental Testimony of Suzie Rose at p. 3.

⁸ Unless otherwise noted, references to “supplemental testimony” herein refer to testimony filed by parties on January 22, 2016.

EXHIBIT 9-A

1 relation to the GWR Determination. ORA reserves the right to contest the reasonableness
2 of all MPWSP costs, including costs related to the updates provided in compliance with
3 the ALJ Ruling, in future filings and cost recovery assessments.

II. SUMMARY OF FINDINGS AND RECOMMENDATIONS

4 Based on supplemental testimony submitted by parties on January 22, 2016,
5
6 ORA provides the following findings regarding the GWR Determination:

- 7 A. Supplemental testimony demonstrates that GWR has met the first
8 eight findings detailed in the Settlement Agreement.
9
- 10 B. Supplemental testimony demonstrates that GWR coupled with a
11 6.4 MGD desalination plant provides numerous positive benefits
12 in comparison to a 9.6 MGD desalination plant.
13
- 14 C. The GWR Project and the Desalination Project currently have
15 differing levels of certainty.
16
- 17 D. There is no projected debt equivalence associated with Cal Am
18 entering into the WPA for GWR Project water.
19
- 20 E. There are inconsistencies in MPWMD and Cal Am cost analyses.
21
- 22 F. Cost analyses submitted in Supplemental Testimony indicate
23 that, compared to the 9.6 MGD Desalination Plant, the 6.4 MGD
24 Desalination Plant with GWR project would likely result in: 1) a
25 small first year revenue requirement premium; and 2) either a
26 small net present value (NPV) premium or small NPV benefit.
27
- 28 G. The ninth finding required by the Settlement Agreement has not
29 been met.
30
- 31 H. The terms set forth in the Settlement Agreement as prerequisites
32 for Cal Am entering into a Water Purchase Agreement (WPA)
33 for GWR water have not yet been met, but could be met by
34 modifying the WPA.
35

36 Based on these findings, ORA recommends that:
37

EXHIBIT 9-A

- 1 I. The Commission should authorize Cal Am to enter into the WPA
2 for GWR if and only if the WPA is modified such that: 1) the
3 language deeming all costs just and reasonable is removed, and
4 2) a reasonable and prudent cost cap is provided for the initial
5 purchase price of the GWR water.

6 **III. DISCUSSION OF FINDINGS**

7 **A. Supplemental testimony demonstrates that GWR has met** 8 **the first eight findings of the Settlement Agreement.**

9 In the MPWSP Settlement Agreement, the settling parties agreed that the
10 Commission should base the GWR Determination on findings related to schedule, cost,
11 benefits, and feasibility. Parties also agreed that that the GWR Determination requires
12 information that was not available at the time of the signing of the Settlement Agreement,
13 including more detailed information regarding the schedules and designs of the GWR
14 Project and MPWSP desalination plant, and agreements for source and product water for
15 the GWR Project. As a result, the Settlement Agreement sets forth nine findings in
16 regards to the GWR Determination, stating that if all of the findings are made or
17 addressed, then Cal Am should enter into a WPA to purchase GWR water, and build a
18 smaller desalination plant; otherwise, Cal Am should proceed with the larger desalination
19 plant.^{2, 10}

20 Supplemental and opening testimony of multiple parties provide detailed
21 information on the status of the nine findings required by the settlement agreement. After
22 reviewing all filed testimony and attachments, ORA concludes that the first eight findings
23 of the Settlement Agreement have been met at this time. The Supplemental Testimony of

² Settlement Agreement at pp. 5-9.

¹⁰ The Settling Parties' Motion to Approve the Settlement Agreement dated July 31, 2013 summarizes the nine findings at p. 5 as follows: "(1) the GWR Project receives approval pursuant to a Final EIR, (2) adequate progress was made and is expected to continue for obtaining permits for the GWR Project, (3) sufficient legal certainty exists concerning long-term viability for GWR source water, (4) there is a lack of evidence showing health and water quality regulators will deny permits or approval, (5) the GWR Project is on schedule for completion, (6) the GWR Project's design is at the required level, (7) a sufficiently detailed funding plan is in place, (8) terms to a Water Purchase Agreement ("WPA") have been agreed to, and (9) the revenue requirement for the combination smaller plant/GWR is just and reasonable compared with the larger plant. A revenue requirement premium for the combination smaller plant/GWR may be just and reasonable if the combination affords significant benefits (including scheduling, diversification of water supply, and environmental benefits) over the larger plant."

EXHIBIT 9-A

Richard Svindland provides a list of these eight findings¹¹ with details on how each finding is satisfied. MRWPCA's Opening Testimony provide additional detail on findings number one through seven,¹² and the Supplemental Testimony of Robert MacLean and David Stoldt provide additional detail on finding number eight, including providing the agreed-upon WPA.¹³

B. Supplemental Testimony demonstrates that GWR coupled with a 6.4 MGD desalination plant provides numerous positive benefits in comparison to a 9.6 MGD desalination plant.

ORA's Supplemental Testimony recommended that the Commission evaluate and consider numerous non-monetary factors and externalities with regard to the GWR Determination. The Settlement Agreement states that parties agree that a revenue requirement premium for the combination of the GWR Project and a smaller MPWSP desalination project ("GWR/Small Desal Option") may be determined just and reasonable, if it affords significant net benefits in comparison to a larger desalination project ("Large Desal Option") when externalities are considered. The Settlement Agreement lists positive benefits that could support the Commission's approval of such a premium, including: (i) a material schedule advantage in that the GWR Project is anticipated to be operable sooner than the desalination plant; (ii) water supply resilience and reliability (benefit of the portfolio approach); and (iii) other positive externalities of the GWR Project, including, but not limited to reduced atmospheric carbon emissions, reduced brine discharge, and the implementation and encouragement of State policies regarding water recycling through early adoption of a water reuse project.¹⁴

¹¹ Supplemental Testimony of Richard Svindland at pp. 3-5.

¹² Opening Testimony of Paul Sciuto addresses findings 1, 3, 5, and 7, Opening Testimony of Alison Imamura addresses finding 2, Opening Testimony of Margaret Nellor addresses finding 4, and Opening Testimony of Robert Holden addresses finding 6.

¹³ Supplemental Testimony of Robert MacLean, Attachment 1; and Supplemental Testimony of David Stoldt, Attachment 4.

¹⁴ Settlement Agreement at p. 7.

1. Positive Benefits Addressed in Parties' Testimony

Testimony of multiple parties address the positive benefits of the GWR/Small Desal option in comparison to the Large Desal Option. These benefits include:

- The material schedule advantage of the GWR Project. The GWR Project is anticipated to be operable significantly sooner than the desalination plant,¹⁵ resulting in reduced withdrawals from the Carmel River at an earlier date,¹⁶ and the possibility of more leniency from the State Water Resources Control Board regarding the Cease and Desist Order ("CDO") deadline.¹⁷
- The additional water supply resilience and reliability of the portfolio approach provided by inclusion of the GWR Project in the MPWSP.¹⁸
- Furthering State goals regarding recycled water.¹⁹
- Environmental benefits and other positive externalities, including reduction of pumping from the Salinas Groundwater Basin, reduction of runoff into the Monterey Bay, reduction of pollutant loads to the lower Salinas watershed, combatting seawater intrusion in the Seaside Groundwater Basin, reduced brine discharge, and reduced GHG emissions.^{20 21}

¹⁵ The Opening Testimony of Paul Sciuto states at p.11 that Cal Am should be able to start extraction of GWR Water in Q1 of 2018, and states at p.12 that the current projected in-service date for the MPWSP is Q2 of 2019. Attachment H of Sciuto's testimony provides a detailed schedule for the GWR Project. The Supplemental Testimony of Richard Svindland states at p. 6 that the GWR Project is projected to be 4-10 months ahead of the current MPWSP schedule, assuming a CPCN is issued in 2016. However, a recent notice sent by Ken Lewis of the Commission's Energy Division updated the schedule, indicating that the EIR/EIS process will not be concluded until November 2017, so it is likely that a CPCN will not be issued until 2018.

¹⁶ Ibid. at p. 6 and 12.

¹⁷ Opening Testimony of Paul Sciuto at pp. 6-7, Supplemental Testimony of Jason Burnett at p.6.

¹⁸ Opening Testimony of Paul Sciuto at p. 6

¹⁹ Supplemental Testimony of David Stoldt at pp. 7-10, Supplemental Testimony of Jason Burnett at p. 7, and Attachment 3 to Burnett's testimony.

²⁰ Opening Testimony of Paul Sciuto at p. 6, GWR Final EIR.

²¹ The Direct Testimony of Dennis Bruce, which presents HDR, Inc.'s economic evaluation of GWR externalities. While the positive externalities examined in the study do benefit Cal Am ratepayers, the financial benefits quantified in the HDR study would not accrue exclusively to Cal Am ratepayers. Because only a portion of the financial benefit associated with these externalities would accrue to Cal Am ratepayers, the quantification in the HDR study should not be viewed as a direct offset to a GWR premium. The benefits should be considered, but not as a direct offset.

EXHIBIT 9-A

1 ORA concurs that these are positive benefits of the GWR/Small Desal option in
2 comparison to the Large Desal Option.

3 2. Positive Benefit with Regards to Return Water 4 Uncertainty

5 In addition to the positive benefits discussed in parties' testimonies and
6 summarized above, the GWR/Small Desal Option also reduces the uncertainties
7 associated with the "return water" percentage. Return water is the amount of water,
8 per the Agency Act, that that is required to remain in the Salinas River Groundwater
9 Basin (SRGB). The volume of return water will be equal to the percentage of SRGB
10 groundwater in the total MPWSP source water production, as determined by the
11 Monterey County Water Resources Agency.²²

12 As discussed in more detail in ORA's Supplemental Testimony,²³ the exact
13 amount of return water necessary for the desalination projects remains uncertain.
14 According to the Return Water Planning Term Sheet, Cal Am will sell the return water at
15 a significantly reduced cost to the Castroville Community Services District (CCSD) for
16 \$110/acre-foot and to the Castroville Seawater Intrusion Project (CSIP) for "an amount
17 equal to the CSIP ratepayers' marginal avoided cost for recycled water produced for use
18 by the CSIP in lieu recharge project's ratepayers." The higher the return water
19 percentage, the more return water will be provided to CCSD and CSIP at this
20 significantly reduced cost.

21 While the return water *percentage* remains equally uncertain in the GWR/Small
22 Desal Option as compared to the Large Desal Option, the *total amount* of return water
23 would always be lower for the GWR/Small Desal Option. Therefore, the impact of the
24 uncertainty of the return water percentage is reduced in the GWR/Small Desal project
25 scenario.

²² Supplemental Testimony of Richard Svindland, Attachment 4 - Return Water Planning Term Sheet, at p. 2.

²³ Supplemental Testimony of Suzie Rose, at pp. 6-8.

EXHIBIT 9-A

1 The impact of this uncertainty is demonstrated in tables provided in the
2 Supplemental Testimony of Richard Svindland, which summarize the “excess supply”
3 (or lack thereof) for various return water percentages and demand scenarios.²⁴ When the
4 return water percentage increases and/or the demand increases, the excess supply
5 decreases. In certain scenarios, there is a risk of a production shortfall for one or both
6 project options. However, in each and every scenario, the GWR/Small Desal Option has
7 a higher amount of “excess supply” than the Large Desal Option. As the tables show, the
8 GWR/Small Desal Option is less impacted by return water percentage uncertainties, and
9 provides reduced risk of production shortfall at higher demand scenarios compared to the
10 Large Desal Option.

11 ORA specifically identified the return water percentage as an area of uncertainty
12 in its Supplemental Testimony due to test well data showing higher salinity levels
13 (and therefore a potentially greater return water requirement) than initially anticipated by
14 Cal Am for the production wells.²⁵ However, the positive benefit discussed above in
15 relation to return water uncertainty also applies to: 1) other issues that could impact the
16 ability of the desalination plant and/or production wells to perform at currently
17 anticipated levels, and 2) higher than anticipated demand. Essentially, the tables
18 discussed above demonstrate that the diversified water supply portfolio associated with
19 the GWR/Small Desal Option will provide additional resiliency in the event that the
20 desalination plant or production wells do not perform as well as currently anticipated,
21 and/or the event that future demand is higher than currently projected. This represents a
22 significant positive benefit of the GWR/Small Desal Option in comparison to the Large
23 Desal Option.

²⁴ Supplemental Testimony of Richard Svindland at p. 10 and Attachment 1.

²⁵ Supplemental Testimony of Suzie Rose at p. 9.

C. The GWR Project and the Desalination Project Currently have differing levels of certainty.

There are numerous uncertainties associated with both the desalination projects and the GWR project. These uncertainties could significantly impact the cost of the alternatives to ratepayers, and should therefore be considered when evaluating the GWR Determination. By definition, it is impossible to know if and how much the uncertainties will impact cost. However, for the purposes of the GWR Determination, it is important to consider the potential for some of these uncertainties to result in costs to ratepayers separate and significantly higher than the current estimated construction costs. Accordingly, it is important to compare the relative uncertainties associated with the GWR Project and the desalination project,²⁶ which include:

1. Schedule

The GWR Project has a certified and unchallenged EIR,²⁷ as opposed to the Desalination Project, for which the CPUC is currently preparing a DEIR. Unexpected delays due to legal challenge or other barriers in project construction are generally less likely to occur once a project has a certified and unchallenged EIR. The MPWSP has experienced significant delay regarding its environmental review, the latest being a delay of the completion of the environmental review process until November 2017.²⁸ Therefore, at this time the GWR Project has a higher level of schedule certainty than the desalination project. Unexpected delays could result in additional costs to ratepayers, particularly if penalties assessed by the SWRCB in relation to the CDO were levied on Cal Am ratepayers.

²⁶ Similar to the discussion of return water uncertainties above, uncertainties associated with the desalination plant apply to both the GWR/Small Desal Option and the Large Desal Option. However, the uncertainties associated with the desalination plant play a smaller role in the GWR/Small Desal Option than the Large Desal Option.

²⁷ Supplemental Testimony of Paul Sciuto at pp. 7-8.

²⁸ March 17, 2016 Energy Division Notice regarding the MPWSP EIR/EIS Schedule.

1 **2. Unexpected Issues Necessitating Changes in Design**

2 Unexpected issues such as legal challenge, return water issues, mitigation
3 measures, and/or unexpected delays can necessitate potentially costly design changes.
4 The likelihood of unexpected issues necessitating costly design changes is generally
5 reduced with a certified and unchallenged EIR. Therefore, with regards to this issue, the
6 GWR Project provides greater cost certainty than the desalination project.

7 **3. Construction Costs**

8 The GWR Project is currently at a 10% design level, and has not yet gone out to
9 bid.²⁹ Cal Am has “final bids in hand for the components of the desalination plant and
10 Cal-Am Only Facilities.”³⁰ Therefore, GWR likely has less construction cost certainty
11 associated with the existing design than the desalination project. Cal Am’s pipeline bid
12 amounts were significantly higher than the estimated amounts, as were the bid amounts
13 for the 6.4 MGD desalination plant.³¹ It is possible that bid prices for the GWR Project
14 could also be higher than the estimated amounts. Based on information from Cal Am’s
15 bidding process for the MPWSP pipelines and plant, Rich Svindland evaluated similar
16 components for the GWR project, and believes that the capital costs for the GWR Project
17 may be understated by approximately \$21 million.³² This amount would represent a
18 construction cost increase of 29% for the GWR Project.³³ At this point in time, the GWR
19 Project has a lower level of cost certainty associated with the existing design compared to
20 the desalination plant.

21 **4. Cost Overruns**

22 Despite the many advantages for GWR discussed above, the GWR/Small Desal
23 Option poses significant risk and uncertainty to Cal Am ratepayers due to the structure of

²⁹ Opening Testimony of Robert Holden at pp. 2-3.

³⁰ Supplemental Testimony of Jeff Linam at p. 5.

³¹ December 15, 2015 Supplemental Testimony of Rich Svindland at p. 4.

³² Supplemental Testimony of Rich Svindland at p. 6.

³³ The Supplemental Testimony of David Stoldt lists a total project budget of \$72,244,146 at p. 16.

EXHIBIT 9-A

1 the WPA agreement. The WPA currently does not provide a defined purchase price for
2 GWR water. Rather, the WPA sets the cost of GWR water as the sum of the Fixed
3 Project Costs³⁴ and Project Operation and Maintenance (O&M) Expenses³⁵ divided by
4 the amount of water produced,³⁶ with no limit on the final cost that may be passed on to
5 ratepayers. Additionally, the WPA states that *all* fixed and O&M costs incurred by
6 MRWPCA and MPWMD in pursuit of the GWR project “shall be deemed reasonable and
7 prudent and the CPUC, by its approval of this Agreement, shall be deemed to have
8 agreed that such costs are reasonable and prudent.”³⁷

9 In contrast, the Large Desal Option has cost caps defined in the Settlement
10 Agreement. While the cost of construction for the desalination plant may exceed the caps
11 in the settlement agreement, the CPUC has jurisdiction over Cal Am’s recovery of those
12 costs from ratepayers, and can deny Cal Am recovery of costs incurred that are not just
13 and reasonable.

14 The structure of the WPA in regards to the purchase price of the GWR water and
15 the lack of a cost cap for that purchase price creates a significant and worrisome
16 difference in the uncertainty of costs associated with the GWR Project when compared to
17 the Large Desal Option.

18 **D. There are inconsistencies in MPWMD and Cal Am cost**
19 **analyses.**

20 MPWMD and Cal Am each present comparative cost analyses for the GWR
21 Determination, including analysis of the revenue requirement for each option, and the net

³⁴ Defined in the WPA at p. 4 as “all pre-construction, development, and capital costs of the Project, including debt service and reserves for the payment of debt service, incurred by the Agency or District.”

³⁵ Defined in the WPA at p. 5 as “all expenses and costs of management, operation, maintenance, repair, replacement, renovation, or improvement of the Project incurred by the Agency and the District, including overhead costs, and properly chargeable to the Project in accordance with generally accepted accounting principles, including, without limitation (a) salaries, wages, and benefits of employees, contracts for professional services, power, chemicals, supplies, insurance, and taxes; (b) an allowance for depreciation, amortization, and obsolescence; (c) all administrative expenses; and (d) a reserve for contingencies, in each case incurred by the Agency or District with respect to the Project.”

³⁶ The WPA details on how the purchase price will be calculated at p. 11.

³⁷ WPA at p. 11.

EXHIBIT 9-A

1 present value (“NPV”) for each option.³⁸ In examining the analyses, assumptions, and
2 cost model³⁹ used to generate the revenue requirement and NPV, ORA finds the
3 following inconsistencies and oversights:

1. NPV Power Escalation

4 Cal Am’s “baseline” analysis of NPV assumes a power cost escalation factor of
5 3%.⁴⁰ However, in performing the NPV analysis, Cal Am used a power cost escalation
6 factor of 3% for the O&M costs associated with the 6.4 and
7 9.6 MGD desalination plants, but a 4.8% power cost escalation factor for the O&M costs
8 associated with GWR.⁴¹ Correcting this error results in a slightly lower NPV for the
9 GWR/Small Desal Option.⁴²
10

2. Version of Cost Model used in MPWMD Analysis

11 MPWMD’s analysis was performed using the December version of the cost
12 model, and does not yet include the model updates discussed in the Supplemental
13 Testimony of Jeff Linam.⁴³ Including these updates slightly increases the cost of the
14 GWR/Small Desal Option.
15

3. 6.4 MGD Capital Cost Scenarios

16 The cost model provides a “most probable capital scenario” and “high end capital
17 scenario” for both the 6.4 MGD and 9.6 desalination plant options. The model refers to
18 the “most probable” scenario as the “soft cap” and the “high end” scenario as the “hard
19 cap” for each desalination plant option. The Settlement Agreement provides cost caps for
20 each desalination plant option. Per the terms of the Settlement Agreement, Cal Am may
21

³⁸ Cal Am’s analysis is presented in the Supplemental Testimony of Jeff Linam, and MPWMD’s analysis is presented in the Supplemental Testimony of David Stoldt.

³⁹ 2015 Monterey Desalination Model v8.4.xls (“cost model”), provided via e-mail to ORA by Jeff Linam in response to ORA’s informal request.

⁴⁰ Supplemental Testimony of Jeff Linam at p. 10.

⁴¹ Cost model, “GWR O&M” tab, cell B38.

⁴² This error likely exists for all the scenarios presented in Attachment 4 of the Supplemental Testimony of Jeff Linam.

⁴³ Supplemental Testimony of Jeff Linam at p.3.

EXHIBIT 9-A

1 seek recovery of reasonable and prudent costs above the caps by filing a Tier 2 advice
2 letter for aggregate costs below specified amounts, and via a petition for modification for
3 recovery above those specified amounts.⁴⁴ In the model, for the 9.6 MGD option, the
4 aggregate “soft cap” scenario falls below the cost caps established in the Settlement
5 Agreement, and the aggregate “hard cap” scenario falls below amount necessitating a
6 petition for modification. However, for the 6.4 MGD option, the “soft cap” scenario
7 exceeds the cost caps in the Settlement Agreement, and the “hard cap” scenario exceeds
8 the amount necessitating a petition for modification.⁴⁵

9 While it is possible that Cal Am would be able to recover reasonable and prudent
10 costs above the cost caps from ratepayers, these costs would be subject to additional
11 scrutiny, including the questions raised in the Supplemental Testimony of David Stoldt
12 regarding the possibility that additional costs were incurred in constructing the 6.4 MGD
13 plant as a result of sizing for future growth.⁴⁶ Because of this, it may not be accurate to
14 compare the costs currently provided in the model for the 6.4 MGD scenario (which
15 exceed the respective “soft” and “hard” caps in the Settlement Agreement) to the costs
16 currently provided in the model for the 9.6 MGD scenario (which do not exceed the
17 respective caps in the Settlement Agreement). Evaluating the 6.4 MGD desalination
18 plant at the cost caps provided in the Settlement Agreement would decrease the estimated
19 cost of the GWR/Small Desal Option.

⁴⁴ Settlement Agreement, pp.12-13, provides aggregate cost caps for the 6.4 MGD plant and Cal Am Only Facilities as \$295.66M, and for the 9.6 MGD plant and Cal Am Only Facilities as \$338.40. Above these amounts, a Tier 2 Advice Letter would be necessary. Aggregate amounts above which a petition for modification would be necessary are \$330.38M for the 6.4 MGD plant and \$384.68M for the 9.6 MGD plant.

⁴⁵ The “soft cap” scenario in the cost model shows \$102.60M for the Cal Am Only Facilities (“assumptions” tab, cell M8) and \$219.30M for the 6.4 MGD plant (“assumptions” tab, cell M7), totaling \$321.90M. The “hard cap” scenario in the cost model shows \$115.4M for the Cal Am Only Facilities (“assumptions” tab, cell M8) and \$234.4M for the 6.4 MGD plant (“assumptions” tab, cell M7), totaling \$349.8M.

⁴⁶ Supplemental Testimony of David Stoldt at pp.12-13.

4. Debt Rate for MCWD Pipeline

The cost model lists the debt rate for the MCWD pipeline as 1.0%.⁴⁷ However, discussions with MPWMD⁴⁸ indicate that the debt rate for this pipeline would be 1.8%, at a minimum.⁴⁹ Correcting this slightly increases the estimated cost of the GWR/Small Desal Option.

5. Outfall Rental Costs

The terms of the WPA will only become binding once Cal Am and MRWPCA execute an agreement for a long term outfall capacity rights lease.⁵⁰ Cal Am and MRWPCA have “barely begun” negotiations for this agreement.⁵¹ The NPV analysis in the cost model includes a line item for “outfall rental”.⁵² This outfall rental cost is included in the NPV analyses, however it is not included in the revenue requirements as calculated by the cost model. The Supplemental Testimony of David Stoldt lists this item as an omission in the revenue requirement calculations,⁵³ however the Supplemental Testimony of Richard Svindland indicates that this cost is covered in the O&M cost estimates.⁵⁴ It is unclear if the outfall rental is double-counted in the NPV analyses (as indicated by Svindland) or left out of the revenue requirement calculations (as indicated by Stoldt).

⁴⁷ Cost Model, “assumptions” tab, cells F91 and G91.

⁴⁸ 2/24/16 ORA conference call with MPWMD.

⁴⁹ If the project qualifies for a State Revolving Fund loan. If the project does not qualify, the rate would likely be higher.

⁵⁰ Whereby MRWPCA leases a portion of the capacity in its ocean outfall to Cal Am for brine discharge from the desalination plant; WPA at p. 18.

⁵¹ Supplemental Testimony of David Stoldt at p. 14.

⁵² Cost Model, “GWR v Desal Comparison – CAW,” “Project Variant (GWR+6.4 MGD),” and “9.6 MGD Desal” tabs.

⁵³ Supplemental Testimony of David Stoldt at p. 14.

⁵⁴ Supplemental Testimony of Richard Svindland at p. 14.

E. The WPA would not trigger debt equivalence for Cal Am.

The Supplemental Testimony of Jeff Linam contemplates the possibility that the WPA for the GWR project may trigger debt equivalence for Cal Am.⁵⁵ Due to the structure of the WPA, Linam concludes that “debt equivalence, if an issue, would appear to be significantly reduced and California American Water would not request a revenue offset at this time.”⁵⁶ Accordingly, Cal Am does not include any projected debt equivalence in its cost projections for the GWR/Small Desal Option. The Supplemental Testimony of David Stoldt provides further detail and explanation as to why the WPA for the GWR project would not trigger debt equivalence for Cal Am.⁵⁷

As both Linam and Stoldt discuss, the WPA is not a take-or-pay contract. Therefore, Cal Am does not have a fixed payment obligation. This fact alone is enough to conclude that the WPA should not trigger debt equivalence for Cal Am, and that no revenue requirement offset is needed in regards to the WPA at this time, or at any time in the future.

F. Cost analyses submitted in Supplemental Testimony indicate that, compared to the Large Desal Option, the GWR/Small Desal Option would likely result in:
1) a small first year revenue requirement premium; and
2) either a small NPV premium or small NPV benefit.

Cal Am and MPWMD provide comparative analyses for a variety of scenarios for the GWR Determination, including analyses of potential first year revenue requirement differentials, NPV differentials, and bill impacts.⁵⁸ Cal Am and MPWMD each provide sensitivity analyses for a variety of factors, including the assumed discount rate and energy escalation rate. The differential in first year revenue requirement and NPV for the two options differ by scenario. Cal Am primarily makes use of the MPWMD Median

⁵⁵ Supplemental Testimony of Jeff Linam at pp. 13-19.

⁵⁶ Supplemental Testimony of Jeff Linam at p. 19.

⁵⁷ Supplemental Testimony of David Stoldt at pp. 28-30.

⁵⁸ Cal Am’s analysis is presented in the Supplemental Testimony of Jeff Linam, and MPWMD’s analysis is presented in the Supplemental Testimony of David Stoldt.

EXHIBIT 9-A

1 Cost Scenario and the Cal Am Most Probable Capital Scenario, and provides a sensitivity
2 analysis by varying one variable at a time based on this scenario.⁵⁹ MPWMD makes use
3 of the Cal Am Most Probable Capital Scenario, comparing this to the NPV for the
4 MPWMD Low and Median Cost Scenarios, and providing a sensitivity analyses when
5 compared to the Median Cost Scenario.⁶⁰ Neither Cal Am nor MPWMD provide
6 comparisons to the High End Cost Scenario for desalination, although Cal Am presents
7 an analysis of its baseline scenarios with a slant well salinity of 92.5%,⁶¹ which is the
8 approximate current salinity of the existing test well.⁶²

9 As noted by Jason Burnett,⁶³ most scenarios show a higher NPV, a higher first
10 year revenue requirement, and a higher average residential bill with the inclusion of
11 GWR. Some scenarios result in a lower NPV and/or lower average residential bill for the
12 GWR/Small Desal Option, however none of the scenarios presented result in a lower first
13 year revenue requirement.⁶⁴ The baseline scenario for Cal Am's analysis results in
14 approximately a 5% NPV increase in 30-yr lifecycle costs for the GWR/Small Desal
15 Option.⁶⁵ MPWMD's analysis of the GWR Low Cost Scenario shows a 0.5% NPV
16 decrease in the 30-yr lifecycle costs for the GWR/Small Desal Option.⁶⁶ Cal Am's
17 average residential bill analysis shows an increase of approximately \$1 or 1% for the

⁵⁹ Supplemental Testimony of Jeff Linam, Attachment 4.

⁶⁰ Supplemental Testimony of David Stoldt at pp. 21-24.

⁶¹ Supplemental Testimony of Jeff Linam, Attachment 5.

⁶² Supplemental Testimony of Richard Svindland at p. 16.

⁶³ Supplemental Testimony of Jason Burnett at p. 5.

⁶⁴ Supplemental Testimony of Jeff Linam, Attachment 4. The Supplemental Testimony of David Stoldt refers to a 1% revenue requirement differential at p.24, but does not provide any additional details on how this number was calculated.

⁶⁵ Attachment 4 to the Supplemental Testimony of Jeff Linam shows a \$33M NPV of the lifecycle differential, and a \$687.3M NPV of the lifecycle costs for the Larger Desal Option.

⁶⁶ Supplemental Testimony of David Stoldt at p. 21 - lists a \$3.4M NPV of the lifecycle savings for the GWR/Smaller Desal Option. The 0.5% savings calculation makes use of the \$687.3M NPV of the lifecycle costs for the Larger Desal Option in the above footnote.

EXHIBIT 9-A

1 baseline scenario. Cal Am's baseline scenario makes use of the GWR Median Cost
2 Scenario, which provides a purchase price of GWR water of \$1,811/acre-ft.⁶⁷

3 With a \$1,600/acre-ft purchase price for the GWR water, Cal Am's analysis shows
4 an average residential bill decrease for the GWR/Small Desal Option of \$1.44 compared
5 to the Large Desal Option.⁶⁸ A \$1,600/acre-ft purchase price for the GWR water also
6 results in a lower NPV for the GWR/Small Desal Option compared to the Large Desal
7 Option, although the first year revenue requirement remains lower for the Large Desal
8 Option.⁶⁹

9 The GWR Low Cost Scenario provides a purchase price for GWR water of
10 \$1,379/acre-ft.⁷⁰ Neither MPWMD nor Cal Am provided a comparative analysis of the
11 first year revenue requirement or the average residential bill for the GWR Low Cost
12 Scenario in supplemental testimony. However, both of these fields would be lower in the
13 GWR Low Cost Scenario than those associated with the \$1,600/acre-ft scenario, for
14 which Cal Am's analysis shows a lower NPV and lower average residential bill for the
15 GWR/Small Desal Option compared to the Large Desal Option.⁷¹ Table 1 summarizes
16 the results of Cal Am and MPWMD's analyses for a few key scenarios.

17

⁶⁷ Supplemental Testimony of David Stoldt at p. 21.

⁶⁸ Supplemental Testimony of Jeff Linam, Attachment 4, shows an average residential bill of \$93.23 for the GWR/Small Desal Option and \$94.67 for the Large Desal Option.

⁶⁹ Supplemental Testimony of Jeff Linam, Attachment 4.

⁷⁰ Supplemental Testimony of David Stoldt at p. 21.

⁷¹ The Supplemental Testimony of David Stoldt discusses the NPV associated with this GWR low cost scenario at p.21, as discussed previously in this section.

EXHIBIT 9-A

1

Table 1. Summary of Cal Am and MPWMD Analyses

Analysis	Purchase Price of GWR Water (/acre-ft)	NPV Increase (5) (6)	Revenue Requirement Increase (7)	Average Residential Bill Increase (7)
Cal Am - Baseline Scenario (1)	\$1,811	4.8%	5.6%	1.1%
MPWMD - Median Cost (2)	\$1,811	3.2%	1% (8)	1% (8)
Cal Am - Baseline with GWR Price Variance (3)	\$1,600	-1.8%	3.9%	-1.5%
MPWMD - Low Cost Scenario (4)	\$1,379	-0.5%	Not Discussed	Not Discussed

(1) Desal Plants at "most probable" scenario, GWR at "median" scenario, energy escalation at 3% for desal and 4.8% for GWR, January version of model

(2) Desal Plants at "most probable" scenario, GWR at "median" scenario, energy escalation at 3% for both, December version of model

(3) All assumptions same as Cal Am baseline except GWR purchase price

(4) Same as MPWMD median, with lower costs associated with GWR Project as described in Supplemental Testimony of David Stoldt at p. 20

(5) NPV of the cumulative NPV Increase for GWR/Small Desal Option over Large Desal Option over 30-yr lifecycle

(6) MPWMD values calculated using NPV increases discussed in the Supplemental Testimony of David Stoldt, divided by the total NPV of Cal Am's baseline scenario

(7) Increase for GWR/Small Desal Option over Large Desal Option

(8) Stated in Supplemental Testimony of David Stoldt at p. 24, with no corresponding calculations

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Ultimately, the NPV, first year revenue requirement, and the average residential bill impact depend on a variety of factors, not all of which were assessed in Cal Am and MPWMD's analyses. Comparing the High End desalination costs to the Low Cost Scenario for GWR would provide favorable results for the GWR/Small Desal Option. If the GWR project receives grant funding,⁷² negotiates more cost-effective energy sources than that which is available to the desalination plant,⁷³ and/or if energy escalation rates are on the higher side,⁷⁴ the GWR/Small Desal Option provides competitive costs, or cost savings, when compared to the Large Desal Option. Additionally, if the return water

⁷² The Supplemental Testimony of Jeff Linam, Attachment 4, provides Cal Am's analysis of the impact of GWR grant funding on NPV, first year revenue requirement, and average residential bills. Grant funding assumptions for the GWR median and low cost scenarios are discussed in the Supplemental Testimony of David Stoldt at p. 20.

⁷³ Supplemental Testimony of David Stoldt at p. 23. This scenario was not assessed in the analyses presented in supplemental testimony.

⁷⁴ The Supplemental Testimony of Jeff Linam, Attachment 4, provides Cal Am's analysis of the impact of energy escalation rates on NPV, first year revenue requirement, and average residential bills. The Supplemental Testimony of David Stoldt at p. 23 provides MPWMD's analysis of the impact of energy escalation rates on NPV.

EXHIBIT 9-A

percentage is higher than expected,⁷⁵ or other uncertainties discussed above result in higher than estimated costs for Cal Am, the GWR/Small Desal Option remains competitive. While it is impossible to determine which of the multitude of scenarios will come to pass, given the cost estimates and range of scenarios presented, it appears likely that in comparison to the Large Desal Option, the GWR/Small Desal Option would result in: 1) a small first year revenue requirement premium; 2) either a small NPV premium or small NPV benefit.

As discussed above, there are numerous uncertainties associated with the Large Desal Option, and numerous positive benefits associated with the GWR/Small Desal Option. There is also the possibility that the GWR/Small Desal Option will provide a NPV and/or average residential bill net benefit in comparison to the Large Desal Option. Because of these factors, the possibility of a small first year revenue requirement premium for the GWR/Small Desal Option, such as that presented in supplemental testimony for the lower-end GWR cost scenarios, would likely be considered reasonable.

G. The ninth finding required by the settlement agreement has not been met absent a defined purchase price or price cap.

The ninth finding of the Settlement Agreement requires that:

“The revenue requirement for the combination of the GWR Project and the smaller desalination project, including the projected debt equivalence for the GWR Project, if any, determined pursuant to Section 4.4, is just and reasonable when compared to the revenue requirement for a larger desalination project alone.”

While, as discussed above, the cost analyses provided in the Supplemental Testimony of David Stoldt and Jeff Linam indicate that the revenue requirement of the GWR/Small Desal Option would likely be comparatively just and reasonable, the WPA does not provide a purchase price or a price cap for the GWR water. The purchase price of the water as specified in the WPA (and discussed in more detail above) would be set at the sum of the fixed project costs and the project O&M expenses, divided by the amount

⁷⁵ Supplemental Testimony of Jeff Linam, Attachment 5.

EXHIBIT 9-A

1 of water produced, with all costs deemed reasonable and prudent. With the GWR Project
2 at just 10% design and no bids in hand, the costs that will be used to calculate the
3 purchase price of the water remain uncertain. The structure of the WPA could burden
4 Cal Am ratepayers with the full impact of all cost overruns, regardless of the amount or
5 cause of the overrun. Given the existing terms of the WPA, the revenue requirement for
6 the GWR/Small Desal Option is currently undefined, and unbounded. The Large Desal
7 Option, in contrast, has cost control measures in place in the Settlement Agreement, and
8 the CPUC maintains jurisdiction over all cost recovery.

9 An undefined and unbounded revenue requirement for the GWR/Small Desal
10 Option cannot be found just and reasonable when compared with the revenue requirement
11 for the Large Desal Option, which has cost caps and cost control measures in place.
12 Therefore, the ninth finding of the Settlement Agreement has not yet been met absent a
13 defined purchase price or price cap.

14 **H. The terms set forth in the settlement agreement as**
15 **prerequisites for Cal Am entering into a WPA for GWR**
16 **water have not yet been met, but could be met with WPA**
17 **modification.**

18 The ninth finding discussed above is listed in the Settlement Agreement as a
19 prerequisite for Cal Am entering into a WPA for GWR water. As discussed above, the
20 ninth finding has not been met. Therefore, the terms set forth in the Settlement
21 Agreement for Cal Am entering into a WPA have not been met.

22 Additionally, the Settlement Agreement states: “The Parties anticipate that the
23 evidentiary hearings in the separate phase will support findings by the Commission of an
24 upper range of reasonableness for the price of GWR Project water for inclusion in the
25 WPA based upon consideration of all positive and negative externalities associated with
26 the GWR Project.”⁷⁶ While evidentiary hearings have not yet begun, no parties provided
27 input to the Commission on an upper range of reasonableness for the price of GWR water
28 in Supplemental Testimony. The Settlement Agreement indicates that this upper range of

⁷⁶ Settlement Agreement at p. 7.

EXHIBIT 9-A

1 reasonableness for the price of the GWR Project water will be included in the WPA,
2 however, the WPA does not currently include this aspect. For this reason, also, the terms
3 set forth in the settlement agreement for Cal Am entering into a WPA have not yet been
4 met.

5 The ninth finding and the terms of the settlement agreement regarding GWR could
6 be met if the WPA were modified such that:

- 7 1) Language deeming all costs just and reasonable is removed from
8 the WPA.
9
- 10 2) A reasonable and prudent cost cap on the price of GWR
11 purchased water is including in the WPA.
12

13 As discussed above, the WPA deems all costs incurred in relation to GWR
14 reasonable and prudent. Specifically, this paragraph states:

15 The Parties agree that, given the status of the Agency and the
16 District as governmental agencies and the requirements under law
17 that they incur only reasonable and prudent costs and expenses for
18 purposes related to their governmental duties and the fact that such
19 costs and expenses are subject to public review and scrutiny, all
20 Fixed Project Costs and Project Operation and Maintenance
21 Expenses incurred by the Agency and the District in compliance
22 with the terms of this Agreement shall be deemed reasonable and
23 prudent *and the CPUC, by its approval of this Agreement, shall be*
24 *deemed to have agreed that such costs are reasonable and*
25 *prudent.*⁷⁷
26

27 This paragraph, in combination with the absence of a cap on the purchase price of
28 the GWR water, provides for an undefined and unbounded revenue requirement, which
29 cannot be found just and reasonable. Removing this language would help ensure that Cal
30 Am ratepayers are not penalized for any unreasonable or imprudent costs incurred by
31 MPWMD or MRWPCA in connection with the GWR project. Including a reasonable
32 and prudent cost cap for the purchase price of GWR water in the WPA would also further
33 this goal.

⁷⁷ WPA at p. 11, emphasis added.

EXHIBIT 9-A

1 Additionally, providing a cost cap in the WPA for the purchase price of GWR
2 water would increase the certainty of cost for the GWR/Small Desal Option above and
3 beyond that of the Large Desal Option. While the Settlement Agreement contains cost
4 caps for both the small and the large desalination plant, these costs are “soft” cost caps
5 not “hard” cost caps – meaning that if the construction costs exceed the caps in the
6 Settlement Agreement, Cal Am can submit an advice letter or petition for modification to
7 the Commission requesting that the additional costs above the cap be funded by
8 ratepayers. While ratepayers might not necessarily shoulder costs above the caps - as the
9 Commission would first need to determine the costs to be just and reasonable - the
10 possibility remains that ratepayers could bear at least a portion of costs above the cost
11 caps in the Settlement Agreement. If the GWR/Small Desal Option included a price cap
12 on the GWR Water purchase price, then this option would provide a higher level of cost
13 certainty than the Large Desal Option, adding another positive benefit that could help
14 justify a revenue requirement and/or NPV premium.

15 The added certainty of cost, in combination with the positive externalities
16 discussed in previous sections, would render a small revenue requirement and NPV
17 premium reasonable for the GWR/Small Desal Option. Therefore, the ninth finding and
18 the terms of the settlement agreement regarding GWR could be met if the language
19 deeming all costs reasonable and prudent were removed from the WPA, and a reasonable
20 and prudent cost cap was included in the WPA to ensure that the any premium was
21 minimal.

IV. RECOMMENDATIONS

22 Based on the above findings, ORA recommends that the Commission authorize
23 Cal Am to enter into the WPA agreement for GWR if and only if the WPA is modified as
24 discussed below.
25

EXHIBIT 9-A

A. Removal of the “Reasonable and Prudent” Language from the WPA

The paragraph in the WPA related to all costs incurred being deemed reasonable and prudent⁷⁸ must be removed from the WPA. Costs cannot be deemed just and reasonable by the CPUC prior to review of those costs. This language must be removed to ensure that Cal Am ratepayers are not unduly burdened with the full impact of any potential cost overruns, regardless of the amount or cause of the overrun.

B. Cost Cap on Purchase Price must be Provided

A reasonable and prudent cap on the purchase price of the GWR water must be provided in the WPA, for the reasons discussed above. Before determining the appropriate cap on the purchase price, the inconsistencies in the cost analyses and in the cost model (discussed above) must be resolved to provide as accurate a comparison as possible.

There are positive benefits associated with the GWR/Small Desal Option in comparison to the Large Desal Option. If a reasonable and prudent cost cap is included for the purchase price of GWR water, there will be increased certainties with regards to the cost of the GWR/Small Desal Option compared to the Large Desal Option. Therefore, if the above conditions are met, a small, defined NPV and revenue requirement premium for the GWR/Small Desal Option above that of the Large Desal Option would be just and reasonable.

If the WPA is modified as discussed above, the Commission should authorize Cal Am to enter into the WPA for GWR water, due to lower levels of uncertainty and the significant positive benefits associated with the GWR/Small Desal Option as compared to the Large Desal Option.

If the WPA is not modified as recommended, the Commission should not authorize Cal Am to enter into the WPA for GWR water, as it poses too great a risk for Cal Am ratepayers.

⁷⁸ WPA at p. 11.

EXHIBIT 9-A

V. CONCLUSION

The Commission should require parties to correct inconsistencies in the cost analyses and in the cost model as discussed herein. Once these corrections are made, a reasonable and prudent cost cap should be established for the purchase price of GWR water. If the WPA is modified: (1) to eliminate language deeming all costs reasonable and prudent, and (2) to include a reasonable and prudent cost cap for the purchase price of GWR water, the Commission should authorize Cal Am to enter into the WPA agreement for GWR.