

BEFORE THE PUBLIC UTILITIES  
COMMISSION OF THE STATE OF CALIFORNIA



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Order Instituting Rulemaking on the  
Commission's own Motion to Consider a  
Comprehensive Policy Framework for  
Recycled Water.

Rulemaking 10-11-014  
(Filed November 19, 2010)

**RESPONSE TO PRE-HEARING CONFERENCE STATEMENTS OF  
THE DIVISION OF RATEPAYER ADVOCATES**

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**I. INTRODUCTION**

Pursuant to Ordering Paragraph 10 of the Order Instituting Rulemaking to consider a comprehensive policy framework for recycled water ("OIR") issued by the Commission on November 23, 2010, the Division of Ratepayer Advocates ("DRA") files its Response to Pre-Hearing Conference Statements ("Response"). DRA's Response includes responses to issues raised by other parties to the OIR as well as a proposal for focusing the scope of the OIR and workshops. As discussed in this Response, DRA recommends that the Commission focus the OIR on goal setting, financing, rate design, and reporting requirements, and that it hold workshops on these topics.

While parties are generally in agreement that State agencies should enhance coordination around recycled water and that the agencies should work to ensure that the Commission's recycled water policies act in concert with other statewide goals (e.g. for energy efficiency and AB 32 compliance), inter-agency coordination on those energy and environmental goals is beyond the reasonable scope of this OIR. As DRA noted in its Pre-Hearing Conference Statement, more data collection will be necessary before the greenhouse-gas impacts of recycled water development can be accurately quantified.<sup>1</sup>

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<sup>1</sup> DRA Pre-Hearing Conference Statement, p. 14.

Thus, DRA recommends that this OIR be scoped to focus on areas where Commission policy can improve investor-owned water utilities' ("IOU") ability to cost-effectively increase recycled water deliveries.

## **II. Response to Pre-Hearing Conference Statements**

DRA's responses include areas of strong agreement or disagreement with other parties' Pre-Hearing Conference statements and are limited to areas DRA would like to see in the scope of the OIR.

### **A. Setting Mandatory Goals for Recycled Water Deliveries is both Useful and Feasible**

Most of the parties opine that the Commission should not set goals for IOU recycled water deliveries. Parties argue that due to the complex and region-specific attributes of recycled water projects, delivery goals would be difficult to develop and even harder to achieve.<sup>2</sup> In addition, the California Water Association ("CWA") contends that goals would have negative consequences for IOUs, ratepayers, and the environment. CWA states that:

"Furthermore, if the Commission independently sets goals for its regulated water utilities, it risks, among other things: (a) setting goals that may be in conflict with future goals that are more beneficial to the local watersheds; (b) prioritizing a source of supply that may prove to be more costly than uses developed through Integrated Regional Water Management Plans ("IRWMPs"); and (c) straining cooperative relationships between the regulated water utilities and their public agency partners."<sup>3</sup>

DRA recognizes that recycled water potential is region-specific and that public agencies are the leads for project development who must secure financing, permits, and other project pre-requisites. Neither of these factors, however, makes IOU recycled water goals infeasible. In some regions, such as the Santa Clarita Valley, public agencies

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<sup>2</sup> See the Pre-Hearing Conference statements of the Sanitation Districts of Los Angeles County, the California Water Association, Santa Clara Valley Water District, and California Water Service Company in response to Question #6 of the OIR.

<sup>3</sup> California Water Association ("CWA") Pre-Hearing Conference Statement, p. 5-6.

have already developed a plan for full wastewater recycling by 2050.<sup>4</sup> Included in this plan is the build-out of Valencia Water Company's ("Valencia") recycled water delivery system. Absent mandatory goals, Valencia would request Commission approval of recycled water projects in each GRC and DRA and the Commission would review those projects on a piecemeal basis. Having mandatory goals, however, would allow for a more comprehensive, longer-term analysis. First, DRA and the Commission would be able to assess Valencia's projected participation in the plan and examine elements of the timing, cost, type, and quantity of recycled water to be delivered. That analysis could strengthen Valencia's role in the plan and form the basis of reasonable goals. Second, GRC review of individual recycled water projects would be informed by goals that correspond to multiple GRC cycles.<sup>5</sup> IOUs would have to justify deviations from the goal timeline and the Commission would be able to see how a recycled water project achieves progress towards the goal.

DRA disagrees with California Water Service Company's ("CWS") statement that there should not be either mandatory or voluntary productions or delivery goals for recycled water.<sup>6</sup> DRA notes that despite CWS' opposition to setting goals, CWS provides examples of how goals could be developed to benefit ratepayers and watersheds. In fact, CWS provided a detailed and thoughtful response to Question #2 (Potential Use of Recycled Water) that shows the recycled water potential for each of its service districts.<sup>7</sup> DRA contends that CWS' analysis makes mandatory goal setting possible and worthwhile. CWS' recycled water development goals would be based upon the potential for recycled water development in certain districts, while other districts with

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<sup>4</sup> Valencia Water Company Pre-Hearing Conference Statement, p. 3.

<sup>5</sup> As DRA stated in its Pre-Hearing Conference Statement, "DRA recommends that the Commission attempt to set goals within the OIR. If goal development requires additional time, then each IOU could present a goal proposal in its next GRC." (p. 3). DRA also proposed setting goals based upon 3-5 GRC cycles. (p. 3). Thus, the Commission could examine a project proposed in one GRC with the knowledge of what other projects may be proposed in subsequent GRCs in order to meet the goals.

<sup>6</sup> California Water Service Company Pre-Hearing Conference Statement, p. 6.

<sup>7</sup> *Id.*, at 5-7.

no current recycled water potential would not be included. CWS' delivery goal would allow for flexibility in that projects delayed or postponed in one district could be offset by projects in other districts. The Commission could also then assess the prioritization of CWS' recycling projects and make adjustments for environmental, economic, or other factors. For example, the Commission could order CWS to prioritize recycling projects in certain Southern California districts in order to reduce reliance on expensive, energy-intensive imported water and adjust CWS' goals accordingly. With clear mandatory goals and a roadmap for how to achieve them, CWS would then have the incentive to work with its public agency partners to advance recycled water projects.

Great Oaks Water Company's ("Great Oaks") response to Question #6 illustrates why this OIR and mandatory goal setting is necessary. Great Oaks does not serve recycled water within its authorized service area. Instead, the City of San Jose serves recycled water within Great Oaks' service area and this has been an issue of contention and controversy between Great Oaks and the City of San Jose.<sup>8</sup> Recently, however, Great Oaks and the City of San Jose have initiated discussions aimed at finding ways to supply additional recycled water in Great Oaks' service territory.<sup>2</sup>

With a mandatory water recycling goal, (should a goal be deemed reasonable), Great Oaks would then have the appropriate incentive to reach agreement with the City of San Jose and the Santa Clara Valley Water District ("SCVWD") on joint recycled water development. In addition, the public agencies would be able to better plan their recycling projects knowing that Great Oaks will be receiving an amount of the recycled water.

SCVWD's responses to the OIR questions show the difference mandatory goals would make. SCVWD has been delivering recycled water to its public agency partners since 1997, and currently delivers 12,000 acre-feet of recycled water annually.<sup>10</sup> To date,

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<sup>8</sup> Pre-Hearing Conference Statement and Responses to Issues and Questions of Great Oaks Water Company, p. 2.

<sup>2</sup> Id.

<sup>10</sup> Santa Clara Valley Water District ("SCVWD") Pre-Hearing Conference Statement, p. 3. SCVWD states that 16,000 acre-feet of recycled water is used annually in Santa Clara County and that the SCVWD partnership with South Bay Water Recycling accounts for 75% of that water. 75% of 16,000 is 12,000.

SCVWD has not delivered a single drop of recycled water to either Great Oaks or San Jose Water Company, the two IOUs in its service area. Setting voluntary goals or no goals at all will not effectively advance IOU contributions to the State Water Resource Control Board's statewide recycling goals.

The aforementioned examples illustrate why CWA's concerns are misplaced. If each IOU develops watershed-specific recycling plans in concert with its public agency partners, and the Commission uses those plans as the basis for goals, then the Commission's goals will be in concert with current watershed management goals. In the future, if watershed managers seek to alter their goals, the IOUs can return to the Commission to seek permission for modifying the recycling goals. In this manner, the recycling goals would not prioritize recycling projects over other, more cost-effective supply options. In addition, IOUs would have to bring projects for approval in GRCs so that cost-effectiveness and reasonableness of the project can be established. Furthermore, DRA submits that setting mandatory goals would foment cooperative relationships between IOUs and public agencies by signaling to public agencies that IOUs will be engaged partners in meeting the public agencies' water recycling targets.

Finally, DRA reiterates its proposal that separate goals be established for potable reuse.<sup>11</sup> Goals for potable reuse (direct and indirect) would allow IOUs to be prepared for receiving potable reuse water when it becomes available. SB 918, passed in 2010, requires the California Department of Public Health and the State Water Resources Control Board to develop criteria for safely using recycled water to supplement groundwater basins and reservoirs.<sup>12</sup> Once those criteria are developed, the number of potable reuse projects is likely to increase. By having a potable reuse goal, the IOUs can plan for ways to cooperate with their public agency partners on potable reuse projects.

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<sup>11</sup> DRA Pre-Hearing Conference Statement, p. 3.

<sup>12</sup> See [http://www.leginfo.ca.gov/pub/09-10/bill/sen/sb\\_0901-0950/sb\\_918\\_bill\\_20100831\\_enrolled.pdf](http://www.leginfo.ca.gov/pub/09-10/bill/sen/sb_0901-0950/sb_918_bill_20100831_enrolled.pdf), accessed February 9, 2011.

## **B. The Commission Should Explore Ways to Make IOUs Eligible for Grants and Financing**

DRA concurs with CWA's response to Question #15 regarding funding, and proposes a workshop in this proceeding dedicated to exploring ways IOUs can qualify for grants and low-cost state and federal financing for recycled water projects. As DRA stated in its Pre-Hearing Conference Statement, "DRA supports making IOUs eligible for the same funding opportunities available to municipal water districts. IOU ratepayers should not have to pay for higher cost recycled water projects just because they live within an IOU's service territory."<sup>13</sup>

## **C. The Commission Should Hold a Workshop(s) to Develop Appropriate Recycled Water Rate Designs**

DRA agrees with the Consumer Federation of California's ("CFC") statement that "it is important to develop policies for recycled water that are consistent with water conservation."<sup>14</sup> While discounts may be necessary to incentivize the use of recycled water, the Commission should not authorize rate designs, such as declining block rates, which encourage excessive or inefficient use of recycled water.

DRA also contends that recycled water rates need not be set at levels lower than potable water rates in all circumstances. Contrary to the assertion by the Sanitation Districts of Los Angeles County ("LA County") that "recycled water rates have had to be set at levels lower than potable water,"<sup>15</sup> California Water Code Section 13580(c) states: "[t]he rate for recycled water shall be comparable to, or less than, the retail water supplier's rate for potable water." A rate design workshop will assist parties to reach consensus on situations where recycled water rates should be comparable to potable water rates.

LA County also states, however, that recycled systems may operate at lower or higher costs than potable water systems. DRA agrees, and notes that the actual operating

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<sup>13</sup> DRA Pre-Hearing Conference Statement, p. 12.

<sup>14</sup> Consumer Federation of California ("CFC") Prehearing Conference Statement, p. 3.

<sup>15</sup> Sanitation Districts of Los Angeles County Prehearing Conference Statement, p. 5

costs of recycled water systems, as well as existing potable water rates, should be taken into consideration when developing rates for recycled water and potable water in the same service areas. For example, in service areas with a separate irrigation customer class, rates for irrigation water may already be higher than rates for potable water in the regular domestic system. In such areas, recycled water could possibly be provided at a cost lower than the irrigation rate without requiring subsidization. DRA recommends that the proposed recycled water rate design workshop allow parties to develop guidelines for rate structures for different customer classes.

#### **D. A Clear Policy on How to Account for Any Lost Revenues is Needed**

Regarding the potential for lost revenues, DRA notes that although Section 13580.8 of the California Water Code allows a water utility to provide recycled water at a discounted rate, this does not necessarily mean that recycled water must be priced at a discount. Section 13580.8(b) states as follows:

“A regulated water utility may request the commission to establish the rate or rates for the delivery of recycled or nonpotable water, with the objective of providing, where practicable, a reasonable economic incentive for the customer to purchase recycled or nonpotable water in place of potable water.”

Furthermore, Section 13580.8(d) states that “[t]he commission shall, as appropriate, provide a discount from the general metered rate of the water utility for potable water ...” Neither of these code sections amount to a requirement that recycled water must be priced below potable water in all circumstances. Where a discount is necessary to incentivize use, the Commission may authorize a discount, and revenue shortfalls may be made up by potable water customers. Thus, CWA’s claim that, “if Commission policy is to promote recycled water, it *must* (emphasis added) be priced at a discount and, if necessary, subsidized through general rates ...”<sup>16</sup> is inaccurate.

DRA agrees with CFC’s statement that the regulatory framework developed in this proceeding should include a policy “...that protects against excessive costs passed down

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<sup>16</sup> CWA Pre-Hearing Conference Statement, p. 13

to current potable water ratepayers as a result of new investments for recycled water.”<sup>17</sup> This policy should include clear guidelines for how any reduction in revenues that occurs as a result of discounts provided to recycled water customers will be addressed. There are two primary scenarios in which utilities might under-recover revenues due to recycled water. One is through the gap between the cost of service to provide recycled water and the rates charged for recycled water. As LA County and CWA note, and the California Water Code allows, this gap can be covered through the rates for general metered service. This can be done in the rate design phase of each utility’s GRC, and should result in revenue neutrality and negate the need for any additional balancing accounts, such as those suggested by CWA.<sup>18</sup>

Great Oaks states that the Commission should allow mechanisms to recover lost revenues via advice letter.<sup>19</sup> However, DRA contends that this should not be necessary if lost revenues are included in the rate design phase of each utility’s GRC. Furthermore, adopting mandatory goals for recycled water deliveries should ensure that utilities are not faced with unanticipated customer shifts from potable to recycled water. Thus, there should not be situations where utilities would “lose” revenues in between GRCs.

The other possibility for under-recovery of revenues is where consumption of recycled water is lower than forecast. Great Oaks states that “utilities should be able to recover lost revenues through a WRAM (when lost revenues are due to lost water sales, whether recycled water or potable water service) or through modified cost balancing accounts (when lost revenues are the result of higher costs due to recycled water infrastructure and service considerations).”<sup>20</sup> Lost revenues due to lower consumption than authorized, or higher purchased water costs than authorized, may not need to be addressed separately for recycled water. Whichever mechanisms are authorized by the

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<sup>17</sup> CFC Pre-Hearing Conference Statement, p. 2.

<sup>18</sup> CWA Pre-Hearing Conference Statement, p. 14.

<sup>19</sup> Great Oaks Water Company Pre-Hearing Conference Statement, p. 5.

<sup>20</sup> *Id.*, p. 11.

Commission to address lost revenues and changes in variable costs due to lower than forecasted potable water sales may also be used to address lost revenues and changes in variable costs due to lower than forecasted recycled water sales. DRA submits that parties could assess these mechanisms in a rate design workshop.

#### **E. The Commission Should Set Reporting Requirements for Recycled Water Development**

DRA agrees with SCVWD's response to Question #7 in that IOUs should be part of regional recycled water plans and IOUs should submit these plans as part of their GRCs.<sup>21</sup> DRA also concurs with SCVWD's response to Question #23 regarding annual reporting requirements.<sup>22</sup> DRA does not recommend that IOUs create separate water recycling plans because that would defeat the purpose of a regional, integrated planning approach.

### **III. CONCLUSION**

In issuing this OIR, the Commission stated that “[w]hile this OIR anticipates that the Commission’s regulation of recycled water will remain for regulatory consideration in distinct General Rate Cases, the principles and guidelines to be addressed in this rulemaking are meant to guide considerations of recycled water in all General Rate Cases.”<sup>23</sup> DRA submits that mandatory recycled water delivery goals should be a key principle developed in this Rulemaking. Mandatory goals will ensure that all Class A and B water utilities are working towards meeting statewide recycling goals and that the Commission can take a perspective on recycled water implementation beyond a single GRC cycle. As DRA has explained, setting mandatory goals is both feasible and in support of cost-effective, integrated regional water management planning. DRA

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<sup>21</sup>In some regions, the water recycling plans will be contained within the Urban Water Management Plan (“UWMP”). In other regions, there may be a separate master water recycling plan, which is referenced in the UWMP.

<sup>22</sup> See SCVWD Pre-Hearing Conference Statement, p. 8.

<sup>23</sup> CPUC, R.10-11-014, Order Instituting a Rulemaking to Consider a Comprehensive Policy Framework for Recycled Water, p. 2.

recommends the Commission schedule a workshop(s) for parties to work cooperatively towards goal development.

DRA also recommends the Commission hold workshops for rate design, financing, and reporting requirements. These workshops will allow parties to set forth all of the key considerations for the Commission's comprehensive policy framework.

DRA looks forward to discussing procedural and substantive issues at the Pre-Hearing Conference on April 7<sup>th</sup>.

Respectfully submitted,

/s/ LINDA BARRERA

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February 15, 2011

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a copy of “**RESPONSE TO PRE HEARING CONFERENCE STATEMENT OF THE DIVISION OF RATEPAYER**” to the official service list in **R.10-11-014** by using the following service:

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Executed on **February 15, 2011** at San Francisco, California.

/s/ JAIME VADO

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