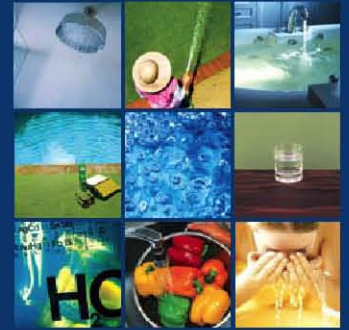


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The Weekly Wrap



January 13, 2012

No. 2012-2

TO: CWA Member Companies
FROM: Jack Hawks, Executive Director
SUBJECT: Highlights for the Week Ending January 13, 2012

AB 550, AB 157 Fail to Move Out of Committee; Sierra Club Drops AB 19—As you know, the Legislature returned from its interim recess on Jan. 4th, and then began the second year of the 2011-2012 legislative session in earnest with numerous hearings from Jan. 9-12. I reported in the Jan. 6th *Weekly Wrap* that a group of 62 public water agencies and local chambers of commerce had sent a letter to Assembly Member (Assm.) Alyson Huber (D-El Dorado Hills) opposing Assembly Bill (AB) 550, which would have prohibited the construction of a peripheral canal around or through the Sacramento-San Joaquin Delta, unless expressly authorized by the Legislature. This past week, on Jan. 10th, the Assembly Water, Parks and Wildlife Committee rejected the bill on a 5-7 vote (five yes, seven no).

Even more emphatically (and perhaps a bit surprising, given the state's budget woes), the Committee voted down Assm. Kevin Jeffries' (R-Riverside) proposal (AB 157) to reduce the total amount of bonds that would be authorized under the Safe, Clean, and Reliable Drinking Water Supply Act of 2012 (the water bond, which is slated for the November ballot) from \$11.1 billion to about \$8.25 billion, by a 1-10 vote. For both bills, seven votes would have been needed for passage.

In her monthly report to the CWA Directors, Legislative Advocate Meg Catzen-Brown reported that regardless of the action on AB 157, the Legislature and the Delta stakeholders are going to continue grappling with the water bond for the next six months. Among the decisions to be made will be to delay to the 2014 ballot, reduce the magnitude of the bond and keep it on the 2012 ballot (but perhaps not across-the-board as AB 157 would have done), or let it go on the 2012 ballot unchanged and see what happens.

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Huber said in news reports that she will not try to revive AB 550 this year, but she will continue to push a provision calling for an independent analysis of financial feasibility prior to construction of any canal. She maintains that the Delta Stewardship Council is moving toward approving a conveyance option and that legislators should make the decision, not appointees. She concluded her comments with an observation on how politically contentious water issues are then made this interesting point: "Ultimately, I think that the Legislature is afraid to be involved in decisions involving water," she said. Two Republicans on the Assembly water committee opposed Huber's bill, along with five Democrats, including four from Southern California.

Another two-year bill of significant interest to CWA members was AB 19 (Fong), a measure sponsored by the Sierra club that originally was going to require metering and/or submetering of multi-unit structures, both residential and mixed use residential and commercial. In an attempt to mollify the low-income renter advocates and the building owners and managers, the Sierra Club amended the bill last week to eliminate the references to submetering (which CWA had succeeded in adding to the bill last year) and simply required metering of new common interest developments. The amended bill was scheduled for hearing on Jan. 10th, but as you can imagine, this new version gave us significant heartburn. During the time, we were communicating our concerns to the author and the Sierra Club, Assm. Fong pulled AB 19 from the Assembly Housing Committee calendar, effectively killing it for the remainder of the year. We will find out when and if the author/sponsor will try again with a new vehicle.

Competitive Bidding Workshop Results in Favorable Direction—California PUC Commissioner Timothy Simon and Administrative law Judge (ALJ) Sean Wilson hosted a workshop Jan. 9th on the Commission's Competitive Bidding Rule (CBR) rulemaking (R.11-03-007). Mercifully, the scheduled two-day affair ended at 2:45 p.m. on the first day, and it appears that the proceeding's new direction is positive. Bob Kelly (Suburban Water), Natalie Wales (Cal Water), Dave Stephenson and Monica Na (California American Water, and I attended some or all of the workshop, although CWA Regulatory Attorneys Marty Mattes and Mari Lane of Nossaman LLP represented CWA on the dais, although the most vocal participants were representatives of the large energy utilities.

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Marty reported to CWA's Regulatory and Finance Committees that three significant outcomes resulted from the workshop discussions. First, with respect to the proposed revision to the CBR that utilities requesting financing authority be required to "make every effort to encourage, assist, recruit, and pre-qualify" diverse business enterprises to serve as lead underwriters or co-managers of debt offerings, several different proposals were made regarding the potential relationship between the CBR and General Order (GO) 156. While there was no objection to the proposed reporting requirement, there were concerns with whether the utilities would be second-guessed as to the vague "make every effort" standard and the equally vague "pre-qualifying" requirement. While GO 156 itself will not be changed as a result of this rulemaking, it appears these concerns will be addressed in whatever final rule is adopted here.

Second, Marty noted that there was a near consensus that the old CBR was of no continuing value and should be abandoned. It was noted that nationwide there had only been one competitively bid debt issuance in the past four years, and none in the past three years. A strong case was made, especially by SoCal Edison, that negotiated debt issuances are competitive in nature, and that the negotiation process typically allows the issuer (the utility) to achieve more favorable terms and lower costs than a competitive bidding procedure would achieve. This point did not fall on deaf ears.

Third, it appears that Commissioner Simon and ALJ Wilson may be receptive to doing away with the CBR in favor of a new "Financing Rule" that will be designed to ensure openness and competitiveness in the selection of debt offerings and in placing debt securities, including a process that will ensure participation by diverse financing entities. CWA made the point that a "Financing Rule" should put the emphasis on general principles that could be applied differently by utilities of different sizes and circumstances so that the water utilities' unique circumstances will be considered (and we can avoid the fate of being treated the same as the energy utilities, an outcome that has not been optimal, to say the least).

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The afternoon session included discussions on the use of debt enhancement features, exemptions, and proposed terms of General Order 24-C (which requires quarterly reporting of receipts and disbursements related to financings). Marty reported that CWA was put on the spot to discuss its proposal of an exemption for issuances of less than \$200 million, with ALJ Wilson noting that our request was far above what inflation would suggest since the last increase to \$20 million in 1986 (i.e., \$1 million). Marty deflected the question to the proposed "Financing Rule," where it should be revisited. It is clear though that Comr Simon is not sympathetic to a large exemption amount, so we will have to work on the draft of the new Financing Rule to make sure the water utility interests on this issue are adequately covered.

With respect to GO 24-B, CWA presented its proposal to require only annual reporting for the water utilities, due to (1) the low frequency of water utilities' financing activities, and (2) because non-publicly traded companies don't make quarterly filings with the SEC. Comr Simon responded by suggesting that quarterly reporting might be maintained for publicly traded companies, but not for those that are privately held.

PG&E's representative opposed the requirement of GO 24-B that utilities maintain separate bank accounts for proceeds of securities issuances, saying that its preferred approach was its current practice of maintaining a master account and then assign funds to sub-accounts for particular projects. The ALJ expressed concern about the apparent current non-compliance with GO 24-B in this regard, but indicated a willingness to consider bringing the GO into conformity with current banking practices.

The workshop concluded with these agreed-upon next steps:

- The remainder of the workshop and evidentiary hearing are canceled.
- The Joint (energy) Utilities will draft, file and serve a proposed workshop report and proposed Financing Rule by Friday, January 20.
- Parties to file and serve opening comments by February 3.
- Parties to file and serve reply comments by February 13.
- The Commissioner and the ALJ thereafter will issue a proposed decision with their own version of a Financing Rule, to be subject to comment on the normal schedule.

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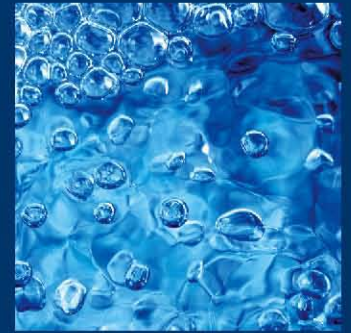


My own take on what will happen is that we'll see from the Joint Utilities draft inclusion of "negotiation" under the "competition" rubric, more specificity regarding "make every effort," substantial revisions to (if not elimination of) the "prequalifying" requirement, a split for the publicly traded and privately held utilities regarding GO 24-B, whatever language the energy utilities want regarding hedging and debt enhancement, and draft Rule 3 regarding GO 156 reporting remaining largely intact. And ... that Comr Simon and ALJ Wilson will go along with most of it (I hope). We'll keep you posted.

Peevey, Florio Host Workshop on System Safety and Ratemaking—As you know, the CPUC is working on multiple fronts to consider and implement the recommendations of the Independent Review Panel and the National Transportation Safety Board that came out of the investigation of the San Bruno natural gas explosion. As part of this effort, the CPUC has established a stakeholder process to solicit ideas and proposals to reform the way safety is considered in the CPUC's ratemaking procedures. It got the public process started with a Jan. 11th workshop hosted by President Mike Peevey and Commissioner Mike Florio that considered a new "straw proposal," which contains various approaches to improve the CPUC's general rate case (GRC) process to prioritize safety initiatives.

While the effort is ostensibly aimed at natural gas pipeline safety, it is clear that if the Commission opens a rulemaking on this subject, all utilities will be involved, including water. PUC Executive Director Paul Clanon said as much in his opening remarks at the workshop. The objective of the straw proposal is to propose improvements to the current ratemaking processes and to elevate and prioritize the regulated utilities' system safety. The workshop broke into groups to discuss how these goals might be accomplished, and to the Commission's credit, the staff kept the workshop on an even keel, with balanced participation on all the tough discussion points.

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A new state law requires each gas corporation to develop a plan for safe and reliable operation of its pipeline facilities. The CPUC must accept, modify, or reject the plan by year-end 2012, and it must allow sufficient flexibility for gas corporations to respond to safety requirements. If the straw proposal morphs into a rulemaking, I can see the PUC extending the “safety plan” requirement to electric, telecom and water utilities.

The main elements of the straw proposal involve changes to rate case proceedings and, again, while they are aimed explicitly at the energy utilities, these proposals could easily extend to water. They include:

- Rigorous analysis and justification of proposed revenue requirements. Utilities should justify increased revenue requirements based on overall spending, prior allocations, and specific explanations on how safety investments are prioritized.
- Requirement of an exhibit from each utility that *details the authorized expenditure from the last GRC versus the actual expenditures* during that period. The exhibit should provide detailed explanations for the revised budgets and should provide accompanying work papers.
- Requirement of an independent audit of the utility’s expenditures included in the exhibit. (And require the utility to pay for the independent auditor)
- Requirement of testimony in the GRC to detail the technical state of the utility system.
- Requirement that the utility’s Chief Operating Officer, along with other relevant employees (including engineers, accountants, internal auditors, etc.), submit testimony detailing the utility’s safety and security policies and practices.
- Requirement that the utility file an independent audit evaluating the utility’s system in terms of implementation of best practices (and the associated metrics) of the security and safety of their electric grid and gas pipelines.
- Requirement that the utility undergo and file an independent management audit that assesses the role that safety plays in the overall culture of the utility, including the use of incentives provided to employees and managers.
- An annual or semi-annual CPUC En Banc Hearing where, among other things, the CEOs of each utility will inform the CPUC of their respective company’s culture and operation in terms of system safety and security.

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- An annual or semi-annual “safety adjustment” proceeding where, among other things:
 - A required audit of the utility’s prioritized list of maintenance and construction projects, as planned and funded in the GRC, with a determination whether the projects were completed.
 - If not completed, did other projects receive priority and have such decisions been justified?
 - Have amounts allocated for safety expenditures remained within that general “bucket”?

Other recommendations involve staff. Specifically:

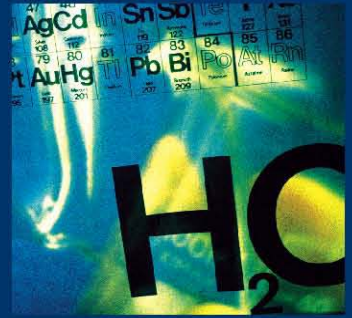
- Institutionalize the CPUC’s Consumer Protection and Safety Division’s (CPSD) role in ratemaking proceedings.
- Ensure that CPSD and DRA share information effectively
- Engineers and trained auditors should work closely together to track dollars spent, projects implemented, and prioritization of these projects within overall safety/risk management assessment.

As you can see, this will be a major rulemaking if the Commission so decides. There will be major questions on whether safety plans become institutionalized within the GRC, whether and how safety data will be disclosed to the public, whether the CPSD will have a formal role like DRA in the GRC, or whether and how safety En Banc hearings will be established. Above all, the overriding issues will be whether and how utility management decisions on safety investments will be reviewed (second-guessed?) and how much flexibility will utilities have with respect to safety investments in their GRCs.

Comr Florio noted that with his and President Peevey’s presence at the workshop, along with three division directors and two ALJs, this effort has a high priority and commitment at the Commission. We’ll keep you posted on future developments.

CPUC Approves Del Oro, San Gabriel Resolutions—At its Jan. 12th Open Meeting, the California PUC took the following actions on the water-related items:

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- **Approved Resolution W-4895**, which grants Del Oro Water's Lime Saddle District an increase in revenues of \$40,544, or 13.67%, for Test Year 2011.
- **Approved Resolution W-4896**, which grants Del Oro Water's Paradise Pines District an increase in revenues of \$222,853, or 13.54%, for Test Year 2011.
- **Held Application 11-02-002**, Suburban Water Systems' General Rate Case Proposed Decision.
- **Approved Decision 12-01-005**, which authorizes Valencia Water to extend its WaterSMART program to dedicated irrigation customers.
- **Held Complaint 09-11-019**, involving establishment of water rates and service conditions for the Sunbird Mobile Home Park.
- **Approved Resolution W-4898**, which finds that Del Oro Water's River Island District has complied with a Commission directive to file plans with the PUC to augment its water supply. Approval of funding and construction of any projects must occur with separate Tier 3 advice letter filings.
- **Held Application 10-04-019**, California American Water's request for cost recovery associated with its lease for the Sand city Desalination Plant.
- **Approved Resolution W-4899**, which rejects San Gabriel Valley Water's request to permit payment of water bills via credit card, debit card or electronic check. SGV Water may seek future authorization via a Tier 3 advice letter.
- **Approved Decision 12-01-016**, extending the statutory deadline for California Water Service's Application 08-05-019 involving discontinuance of its extended service program.
- **Approved Resolution W-4902**, which authorizes Point Arena Water Works to borrow \$120,000 and encumber its assets.
- **Approved Decision 12-01-030**, which provides intervenor compensation of \$107,382 to the Asian Pacific Chamber for its substantial contributions to D.11-05-019, the General Order 156 rulemaking.
- **Approved Decision 12-01-031**, which provides intervenor compensation of \$133,904 to the California Hispanic Chamber of Commerce for its substantial contributions to D.11-05-019, the General Order 156 rulemaking.
- **Held Application 10-09-018**, California American Water's request for authorization to implement the Carmel River Reroute and San Clemente Dam Removal, include cost recovery.

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- **Approved Decision 12-01-036**, which involved the Division of Ratepayer Advocates' request for rehearing in D.10-12-029, involving the disposition of Valencia Water's perchlorate settlement claims of approximately \$3.6 million.

Sandoval, Simon Honored at Latino Leaders Event—CWA Legislative Committee Chair Evan Jacobs of California American Water and I attended the 13th Annual Latino Leaders' Reception for Constitutional Officers, Legislators and Appointees on Jan. 11th in Sacramento. We were pleased to see that both CPUC Commissioners Catherine Sandoval and Timothy Simon were honored with awards. Hosted by the Latino Journal and owner/publisher Jose Perez, who is also chair of the California Utility Diversity Council, the reception draws many legislators and state appointees.

For me, it was especially productive because Evan and I were able to spend time with each commissioner, as well as Comr Sandoval's Chief of Staff Ditas Katague and former Assembly Member Gwen Moore.

New Report Advocates Supply Potential for Recycled Water—A new report from the National Research Council, released on Jan. 10th, says that recent technical advances in treating and reusing municipal wastewater for drinking water, irrigation, industry, and other applications could significantly increase the nation's total available water resources, particularly in coastal areas facing water shortages. The report hastens to add that "new analyses suggest that the possible health risks of exposure to chemical contaminants and disease-causing microbes from wastewater reuse do not exceed, and in some cases may be significantly lower than, the risks of existing water supplies."

The report examines a wide range of reuse applications, including potable water, non-potable urban and industrial uses, irrigation, groundwater recharge, and ecological enhancement. The committee that prepared the report found that many communities have already implemented water reuse projects -- such as irrigating golf courses and parks or providing industrial cooling water in locations near wastewater reclamation plants -- that are well-established and generally accepted.

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The report outlines wastewater treatment technologies for mitigating chemical and microbial contaminants, including both engineered and natural treatment systems. It notes that the concentrations of chemicals and microbial contaminants in reuse projects designed to augment drinking water supplies can be comparable to or lower than those commonly present in many drinking water supplies.

Although the costs of reclaimed water are often higher than current water sources, the report urges water authorities to consider other costs and benefits in addition to monetary expenditures when assessing reuse projects. For example, water reuse systems used in conjunction with a water conservation program could be effective in reducing seasonal peak demands on the drinking water system. Depending on the specific designs and pumping requirements, reuse projects could also have a larger or smaller carbon footprint than existing supply alternatives or reduce water flows to downstream users and ecosystems.

The report notes that existing legislative tools could be applied to improve the quality of water for reuse, including updating the National Pretreatment Program's list of priority pollutants to include a wider inventory of known toxic substances. Also, it lists 14 areas of research to help guide the country on how to apply water reuse appropriately. Such research would require improved coordination among federal and nongovernmental organizations.

The study was sponsored by the U.S. Environmental Protection Agency, U.S. Bureau of Reclamation, National Science Foundation, National Water Research Institute, Centers for Disease Control and Prevention, Water Research Foundation, Orange County Water District, Orange County Sanitation District, Los Angeles Department of Water and Power, Irvine Ranch Water District, West Basin Water District, Inland Empire Utilities Agency, Metropolitan Water District of Southern California, Los Angeles County Sanitation Districts, and Monterey Regional Water Pollution Control Agency. You can access it at http://www.nap.edu/catalog.php?record_id=13303.

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PPIC Issues New Report on Delta Economy—The Public Policy Institute of California (PPIC) issued a new report Jan. 9th titled *Transitions for the Delta Economy*, and it finds that in the first half of the 21st Century, the Delta as a whole is likely to experience a loss of 1 percent of economic activity as a result of what it calls “enormous changes” that are coming to the Delta region.

The study examines the potential economic effects of changes in the Delta land and waterscape as a result of management activities and natural forces and suggests planning priorities to support transitions in the Delta economy. The PPIC authors reviewed recent patterns and trends in Delta land use and employment, and drew on a range of data and modeling tools to assess the effects of several types of physical changes on economic activity in the Delta, including:

1. the permanent flooding of roughly 75,000 acres of land on subsided Delta islands that may not offer sufficient economic justification for repair after flooding;
2. increases in irrigation water salinity from the introduction of dual conveyance, sea level rise, and the flooding of islands that restrict salinity intrusion from the Delta’s western edge; and
3. reductions in cropland from the expansion of seasonal floodplain and tidal marsh habitat.

Most of these changes will directly affect land and water conditions in the Delta’s primary zone—nearly 500,000 acres of largely subsided agricultural lands in the inner Delta, where development is restricted because of high flood risk. Within the first half of this century, the report notes that island flooding, habitat conversions, the introduction of dual conveyance, and sea level rise could generate more than 1,100 direct job losses per year within this zone and annual reductions of over \$80 million in value added—a measure of overall economic activity. Total losses for the wider region—including multiplier effects—may reach 1,800 jobs per year, \$130 million in value added, and nearly \$14 million in state and local tax receipts.

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“Rather than trying to prevent the Delta’s landscape from changing, planning efforts should anticipate and prepare for the likely changes to the region’s land and water resources,” the report notes. “Many changes – including earthquakes, sea level rise, and high flood flows – are inevitable, and management decisions will need to assess how best to respond in ways that use scarce dollars to protect human and environmental uses of the Delta’s land and water resources.”

The report identifies four planning priorities to assist with the transition, including making strategic decisions on where to invest in Delta levee improvements, encouraging growth of nature-based and cultural recreation in the inner Delta, conducting more detailed modeling of the effects of physical changes, and consideration of mitigation actions.

The research was supported with funding from the UC Davis Watershed Sciences Center, and you can get the report at <http://www.ppic.org/main/publication.asp?i=913>.

Upcoming Industry Meetings/Conferences/Events:

- January 18, 2012 – California Water Commission – Public Benefits of Water Storage (9:30a-11:30a; Natural Resources Building; 1416 9th St., Sacramento 95814); J. Hawks may attend.
- January 18, 2012 – Senate Rules Committee - Confirmation Hearing for PUC Commissioners Ferron, Florio and Sandoval (1:30p-4:30p; State Capitol, Room 113, Sacramento 95814); J. Hawks will attend.
- January 19-20, 2011 – Recycled Water OIR Workshop #3 (10:00a-3:00p; CPUC Auditorium; 505 Van Ness Ave., San Francisco 94102); J. Hawks will attend.
- January 19, 2012 - CUWCC/DWR CII Task Force Meeting (9:30a-3:30p; 815 S St., Sacramento 95811).
- January 23-25, 2012 – Evidentiary Hearings in Water Utility Cost-of-Capital Proceeding (10:00a – 4:00p; Commission Hearing Room; 601 Van Ness Ave., San Francisco 94102).

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- January 27, 2012 – Southern California Water Cte. Quarterly Meeting (10:00a – 1:30p; Pacific Palms Hotel; 1 Industry Hills Parkway, Industry, CA 91744).
- February 2, 2012 – Dept. of Water Resources – Water Plan Update 2013 Public Advisory Cte. Meeting (9:00a-4:30p; Cal EPA Building, 1001 I St., Sacramento 95814); J. Hawks will attend.
- February 2, 2012 – California PUC Open Meeting (9: 00a – 12:00p; 505 Van Ness Ave., San Francisco 94102)
- February 5-8, 2012 - National Association of Regulatory Utility Commissioners – Annual Winter Committee Meetings (8:45a-5:15p; Renaissance Hotel; 999 9th St., N.W., Washington, DC 20001); J. Hawks will attend.
- February 9, 2012 – Dept. of Water Resources – CII Task Force Meeting (9:30a – 3:30p; San Diego County Water Authority; 4677 Overland Ave., San Diego 92123); J. Hawks will attend.
- February 10, 2012 - CWA Directors Meeting (9:30a-2:30p; California Water Association, 601 Van Ness Ave., Suite 2047, San Francisco 94102); J. Hawks will attend.
- February 16, 2012 – California PUC Open Meeting (9: 00a – 12:00p; 505 Van Ness Ave., San Francisco 94102)
- March 25-27, 2012 – Water Reuse Association - 2012 WaterReuse California Annual Conference (Sheraton Grand Hotel; 1230 J St., Sacramento, CA 95814; http://www.watereuse.org/sites/default/files/u8/calicon2012_registration.pdf)

—CWA—