

Decision 99-09-016 September 2, 1999

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

In the matter of the Application of the Southern California Water Company (U 133 W) for approval pursuant to Public Utilities Code Sections 454 and 851 of a settlement agreement delineating water rights in the Six Basins and for authority to effect related ratemaking changes in its Claremont District.

Application 98-12-036  
(Filed December 18, 1998)

Patricia A. Schmiede, Attorney at Law, and Susan L. Conway, for Southern California Water Company, applicant.

Peter G. Fairchild, Attorney at Law, and Donald McCrea, for Ratepayer Representation Branch, Water Division, intervenor.

**OPINION**

**1. Summary**

Southern California Water Company (SCWC) seeks approval of its participation in a stipulated judgment for adjudication of water rights in the Six Basins hydrologic area in Los Angeles County and an agreement between SCWC and the City of Claremont regarding water rights, water rates and well easements. The application is opposed by the Ratepayer Representation Branch of the Commission's Water Division (Branch) on grounds that the agreement with the city is disadvantageous to ratepayers. This decision approves the application, with conditions that address some of Branch's concerns.

## **2. Procedural History**

The application, filed on December 18, 1998, is brought pursuant to Pub. Util. Code §§ 454 and 851, which govern proposed rate changes and encumbrances on utility property. Branch timely filed its protest. Prehearing conferences were conducted on March 18 and April 29, 1999, while the parties considered the possibility of settlement. The parties were given until May 25, 1999, to conclude their settlement discussions. When settlement efforts failed, the matter proceeded to hearing on May 25 and 26, 1999. The company presented its evidence through three witnesses, including a Claremont city council member and an assistant city manager. Branch presented evidence through its staff engineer and project manager. Briefing was completed on July 9, 1999, at which time the matter was deemed submitted for decision.

## **3. Background**

SCWC and the City of Claremont, along with nine other parties, have entered into a consensual adjudication in Los Angeles Superior Court to designate their rights to groundwater and water storage within the Six Basins hydrologic area.<sup>1</sup> Six Basins is located primarily in Los Angeles County and is bounded by the San Jose Hills on the south, the Chino Basin on the east, the San Gabriel Mountains on the north, and the Main San Gabriel Basin on the west. It derives its names from six interconnected groundwater basins.

SCWC operates 24 wells in the Six Basins area and uses this water to serve its Claremont District. The Claremont District is located in a suburban area of

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<sup>1</sup> Case No. KC 029152, Los Angeles Superior Court, East District (Pomona). The stipulated judgment is in evidence as Exhibit 5.

Los Angeles and San Bernardino counties. It includes the City of Claremont and portions of the cities of Pomona, Montclair and Upland. Annual sales of 4.7 million cubic feet of water are made to 10,000 customers in the district.

Since the early 1900s, the Pomona Valley Protective Association has managed the Six Basins. The association is a nonprofit corporation operated by water producers in the area, including SCWC, the City of Pomona and the City of Upland. According to testimony at hearing, groundwater production from the Six Basins has exceeded the available safe yield since at least 1993, and the Six Basins have been in a state of overdraft during that time. According to the Superior Court's judgment, if the overdraft is left unchecked, it will result in water shortages, diminished water quality, increased pump lifts and permanent damage to the basins.

In early 1997, a coalition was formed among parties producing water from the Six Basins in order to develop a court-supervised adjudication plan. Various technical and water rights committees met regularly to resolve issues, including rules for more efficient groundwater management. Agreement was reached and a consensual adjudication was filed by SCWC on September 28, 1998 in the Eastern District of the Los Angeles Superior Court. On December 18, 1998, a hearing was held and a stipulated judgment was entered adjudicating the parties' rights to use of groundwater in the Six Basins area.

#### **4. Terms of Stipulated Judgment**

The parties to the stipulated judgment account for all known producers pumping more than 25 acre feet per year. The judgment determines water rights based on average production of each producer during the period 1985 through 1996. The judgment also requires appointment of a watermaster committee comprised of representatives of each party to the judgment.

Prior to the adjudication, SCWC most recently had pumped 9,300 acre feet per year from the Six Basins. Under the judgment, SCWC is entitled to produce 34.741% of the annually determined safe operating yield. In 1999, the safe operating yield has been set at 24,000 acre feet, thus entitling SCWC to pump 8,338 acre feet during the year. Other major users include the City of Pomona (17.22%, or 4,132 acre feet in 1999) and the City of Upland (15.40%, or 3,696 acre feet in 1999). The City of Claremont accepted an allocation of 2.772%, which amounts to 665 acre feet in 1999.

The stipulated judgment requires the watermaster to determine annually the safe operating yield of the Six Basins and to develop an operating plan to include the monitoring and direction of all production, replenishment, replacement and storage of groundwater. SCWC will be charged a proportionate share of administrative costs of the watermaster, and SCWC proposes to treat the assessment as part of its purchased water cost, included in its supply cost balancing account.

## **5. Water Rights Agreement**

In connection with the stipulated judgment, SCWC and the City of Claremont entered into a water rights agreement dated May 26, 1998. Under the agreement, the city grants SCWC an exclusive lease of the city's share of Six Basins water at a rate set at 90% of the rate for replacement water established each year by the watermaster. The lease has an initial term of 30 years, with successive automatic 10-year renewal periods.

According to SCWC, it will always need the city's share of Six Basins water to meet the needs of the Claremont District. The company estimates a total supply need within its Claremont District in 1999 of approximately 11,700 acre feet. The company plans to supply that need from up to five different sources:

(1) its right to pump 8,338 acre feet from Six Basins at no extra charge; (2) its lease of 665 acre feet from the City of Claremont at 90% of the replacement rate; (3) its use of 444 acre feet from Pomona College's rights; (4) overpumping its right in the Six Basins and paying the replacement charge (\$254 per acre foot); and (5) purchasing treated water from Three Valleys Municipal Water District (\$421 per acre foot).

In return for Claremont agreeing to cap its rights at 2.772% and lease that right to the company at the 90% rate, and other concessions, SCWC agreed to a 50% reduction in the commercial rate (Schedule CM-7ML) that it charges for the city's use of water, and to make that rate available for all water used by the city. Currently, the city receives a rate discount of 12% for water used for irrigation. About 90% to 95% of the water purchased by the city is used for irrigation.

The city also granted SCWC an easement, without cost, to drill up to five wells on city-owned property. In return, the city has a right of first refusal to buy or lease land from SCWC's abandoned wells that may be replaced by the new wells.

## **6. Company's Position**

SCWC witness James B. Gallagher, vice president of customer service for the region, testified that the company and other users had concluded that an adjudication was necessary in order to fix the limit of water that could be pumped from the Six Basins and preserve the quantity and quality of water available.

SCWC is the water purveyor for the City of Claremont, which has no water system of its own. Gallagher said that SCWC's agreement with the City of Claremont was part of negotiations intended to reach a consensual adjudication, rather than a litigated one.

Gallagher testified that the city holds an overlying right in the Six Basins, whereas SCWC's water rights are appropriative. Under California water law, overlying rights generally are superior to appropriative rights. (See, e.g., Katz v. Walkinshaw (1903) 141 Cal. 116, 135-36.) The city's overlying rights amount to between 1,400 and 1,600 acre feet, and Gallagher said that SCWC sought to place a cap on the city's share of water because any greater right likely would have come from SCWC's adjudicated share. SCWC also sought to obtain the right to use the city's share in serving the Claremont District.

Gallagher said that the water rights agreement negotiated with the city offers a number of advantages for the company and its ratepayers. First, he said, it avoided litigated adjudication, which he estimated would have cost the company \$1 million in legal and expert witness fees. Second, the company saves 10% of the cost of replacement water by using the city's 2.772% share. Third, the company obtains easements for up to five wells on city-owned property, thus negating the need to purchase property for well sites. Finally, Gallagher said, the company benefits from capping the city's adjudicated water right and avoids the risk of the city obtaining a greater right to water had the adjudication been litigated.

City Councilman Al Leiga, a former Claremont mayor, and Scott G. Miller, assistant city manager, testified that the water rights agreement benefits the city and its residents. They testified that the advantages of the adjudication and water rights agreement include (1) protecting residents' water supply; (2) putting water management under the direction of a judicially directed watermaster; (3) giving the city a voice in water management as a member of the watermaster; (4) using the city's overlying water rights in a manner deemed most beneficial to residents; (5) creating savings for the city in its own water use and creating new

revenue for the city from SCWC's purchase of the city's adjudicated share of water; and (6) avoiding the cost to the city of a contested adjudication.

The city's witnesses testified that the agreement with SCWC was adopted unanimously by the Claremont City Council in a series of public meetings. They testified that, without the agreement, the city might not have agreed to a consensual adjudication of Six Basins water rights, or at least would have sought a substantially greater share of water based on the municipality's overlying rights.

## **7. Position of Branch**

Branch at hearing did not oppose this Commission's approval of SCWC's participation in the stipulated judgment. However, it does contest the company's water rights agreement with the city. Branch witness Donald McCrea, senior utilities engineer and project manager, testified that his analysis suggests that the agreement with Claremont will unfairly shift rate burden from the city to other ratepayers in the Claremont District.

McCrea presented evidence to show that the only immediate financial benefit to SCWC ratepayers is a savings of \$13,500 annually in purchased water costs through the company's purchase of the city's adjudicated share. The city, however, will realize savings of more than \$100,000 a year because of the 50% reduction in its water rates. That revenue requirement would be shifted to ratepayers other than the city in potential violation of Pub. Util. Code § 453(c), which prohibits unreasonable differences in rates between classes of service.

On cross-examination, McCrea acknowledged that ratepayers benefit from avoiding a contested adjudication, from obtaining a discounted rate for Claremont water, and from capping the share of Claremont water. He acknowledged that the easements for five wells could benefit ratepayers. He

noted, however, that SCWC has no plans to drill new wells in Claremont for at least two years and that it has other property on which wells could be built.

Branch had other objections to the water rights agreement. The agreement gives parties a right to terminate if this Commission disapproves any of its terms now or in the future. In the event of termination, there is no protection for SCWC's investment in wells on city property. Branch notes also that SCWC's proposed tariff for the discounted rate available to the city does not contain the requirement in the prior tariff that irrigation be conducted in off-peak hours, when energy rates are lower. Finally, Branch criticizes the lack of a cap on the amount of water SCWC will be required to purchase from the city each year.

On brief, Branch argues that SCWC has failed to justify its participation in the stipulated adjudication because it nowhere explained why it agreed to a base annual production amounting (initially) to 6,705 acre feet when its production has in the past exceeded 9,000 acre feet per year. Branch alleges that SCWC had failed to provide it with historical production figures for parties to the adjudication which would have permitted an evaluation of the allotments.

## **8. Discussion**

This application seeks Commission approval of (1) SCWC's participation in the Superior Court stipulated judgment for adjudication of Six Basins, and (2) the water rights agreement that SCWC negotiated with the City of Claremont in connection with the adjudication. The company seeks authority to revise its Rate Schedule CM-7ML to offer a rate concession to Claremont for water used by the city.

It is clear on this record that the adjudication of the Six Basins area by its 11 major producers was not only reasonable but critically important. Superior Court Judge William O. McVittie found in the judgment that the native safe yield



of the Six Basins area (that is, the amount of water that can be pumped without managed augmentation) has been continuously exceeded for decades. The court added:

"An unmanaged downward decline in water levels is known to have severe adverse impacts on the rights of groundwater producers and groundwater quality, to cause land subsidence and to cause increased pump lifts. Moreover, the Court finds that presently estimated Safe Yield [i.e.; the amount that can be pumped with proper augmentation]..., with the full benefit of the Replenishment carried on by the Parties has been exceeded and if Production is not managed pursuant to this Physical Solution, severe adverse impacts will result." (Exhibit 5, pp. 10-11.)

By having a watermaster committee establish an annual operating safe yield from Six Basins, and by fixing the percentage of safe yield that each of these 11 entities can claim, the parties and the Superior Court have assured for the foreseeable future the quantity and quality of water available to Californians served by the Six Basins. The judgment provides detailed provisions for replacement water when a party exceeds its percentage production, and the Superior Court retains jurisdiction to resolve any dispute that may arise.

Branch on the record does not oppose the adjudication or SCWC's participation in it. It complains that SCWC did not supply Branch with historic water use records of the 11 parties in order to evaluate the company's acceptance of a 34.741% share, but the evidence shows that this data was considered sensitive and was available had Branch been willing to approach the parties individually.

In any event, both the testimony and the Superior Court judgment show that the base annual production right of each of the parties is not a negotiated number, as Branch suggests, but represents an historical average, based on each party's annual production between 1985-1996. The percentage of operating safe yield fixed for SCWC (34.741%) reflects the company's actual production

percentage during the 12-year period. The allotment to the company is more than double that of any other party to the judgment and appears, with supplemental sources, to be sufficient to meet the company's needs.

While it is not entirely clear that approval by this Commission is required for a water company to participate in a Superior Court adjudication of underground aquifers, to the extent such approval is necessary, we grant it.<sup>2</sup> We also approve as reasonable the rights and obligations that the company has assumed as part of that judgment.

We turn next to SCWC's agreement with the City of Claremont, in which the discount on water purchased for city uses would go from 12% to 50%, saving the city \$109,000 in the first year in its cost of water. SCWC argues that this concession was the result of good-faith bargaining necessary to persuade Claremont to join in the consensual adjudication, to cap the city's overlying water right, and to maintain for SCWC the use of the city's right to water at a cost 10% less than replacement water.

Branch argues that the savings to the company in leasing Claremont's share of Six Basins water is only about \$13,500 a year and that other benefits to the company and its ratepayers are illusory, or at least unproven. Those benefits, according to Branch, are outweighed by shifting some \$100,000 annually in revenue requirements to SCWC customers other than the city.

Witnesses for the city argue that the money that the city saves will inure to the benefit of Claremont residents, who comprise virtually all of the SCWC

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<sup>2</sup> Since the adjudication may be viewed as fixing encumbrances on the SCWC system, within the meaning of Pub. Util. Code § 851, the company seeks a finding that its participation in the adjudication is reasonable, lest costs of the adjudication later be challenged on the basis of reasonableness.

ratepayers likely to be affected. Between 90% and 95% of the water purchased by the city is used to irrigate parks, playgrounds and other civic resources, thus enhancing quality of life and property values. The savings and revenue that the city receives under the agreement will help pay for civic improvements, including a new sports park for youngsters. According to the city witnesses, the proposed agreement with SCWC has been reviewed in numerous public meetings, and no resident has opposed it.

While we agree with Branch that many of the claimed ratepayer benefits are hard to quantify financially, that does not mean that the benefits are not real. Capping the city's overlying rights to Six Basins water and securing no-cost easements for up to five replacement wells on city property can mean significant savings for ratepayers. Because the city is built out, the cost of obtaining land to drill a well of sufficient size was estimated at hearing at \$1 million per wellsite. Avoiding litigation of the adjudication saves costs for all parties. The company's cost of litigating the Mojave River Basin in the mid-1990s exceeded \$450,000. (See, Re Southern California Water Company (1994) 57 CPUC2d 580.) Obtaining the city's share of water at 90% of replacement costs saves the company more than \$13,000 per year.

We find on this record that the city's savings in its cost of water does not constitute an unreasonable difference under Pub. Util. Code § 453(c) as to rates between localities or classes of service. The Commission under General Order 96-A(X)(B) permits water companies to provide free or reduced rates to cities and other public entities. The record shows that such discounts are common. SCWC has a reclaimed water rate with a 50% discount in its Metropolitan District, a metered irrigation rate with a 59% discount in its San Dimas District, a metered irrigation rate with a 33% discount in its Santa Maria District, a public park rate

with an 18% discount in its Ojai District, and a metered irrigation rate with a 13% discount in its Orange County District.

Based on the record as a whole, we conclude that the agreement between SCWC and the City of Claremont, when considered in connection with the consensual adjudication, is a reasonable one and is in the best interests of ratepayers.

At Branch's prompting, SCWC and the City of Claremont agreed during hearing to close the termination loophole in the agreement. Our order today memorializes that agreement. Should the agreement terminate while SCWC is operating wells on city-granted easements, SCWC will pay a one-time sum of \$25,000 per utilized easement to maintain the easement for the remaining useful life of the wells.<sup>3</sup> Branch also observed that SCWC's proposed tariff incorporating the city discount rate does not contain previous restrictions limiting time of use for irrigation water to off-peak hours when energy rates are lower. The company and the city apparently have agreed that off-peak restrictions should continue to apply. Our order today requires the restoration of these restrictions for irrigation water.

In Resolution ALJ 176-3008, dated January 20, 1999, the Commission preliminarily categorized this proceeding as ratesetting, and preliminarily determined that hearings were not necessary. In view of the protest filed by the Ratepayer Representation Branch, and the failure of settlement negotiations,

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<sup>3</sup> Specifically, the parties state that SCWC will pay a one-time sum of \$25,000 in 1999 dollars, escalated annually by the non-labor CPI factor determined by the Commission's ORA Monopoly Regulation Branch to the Water Division, per utilized easement to maintain the easement for the remaining useful life of the wells, based on an estimated useful life of 50 years for each well.

public hearing in the matter became necessary. In view of this, it is necessary to alter the preliminary determination regarding hearing in Resolution ALJ 176-3008. We so provide in our order today. We also designate ALJ Walker as principal hearing officer in this proceeding.

The application is granted, subject to the terms and conditions set forth below.

### **9. Comments on Proposed Decision**

The proposed decision of the principal hearing officer in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure.

SCWC in its comments suggests a change in describing its agreement with the City of Claremont regarding rights of the parties in city-granted easements in the event of cancellation of the Water Rights Agreement, and that change has been made in the decision. Branch in its comments disputes the reasonableness of SCWC's agreement with the City of Claremont, arguing that claimed benefits to the company are illusory. We believe that the decision adequately addresses Branch's arguments and that no further change in the decision is warranted.

### **Findings of Fact**

1. SCWC and the City of Claremont, along with nine other parties, have negotiated a stipulated judgment in Los Angeles Superior Court to designate their rights to groundwater in the Six Basins area in Los Angeles County.
2. On December 18, 1998, a stipulated judgment was entered adjudicating the parties' rights to use of groundwater in the Six Basins area.
3. Under the judgment, SCWC is allotted the largest percentage of safe operating yield (34.741%, or 8,338 acre feet in 1999), and is granted five votes on the watermaster board.

4. SCWC will be charged a proportionate share of administrative costs of the watermaster, which will be treated as part of purchased water costs and included in SCWC's supply cost balancing account.

5. In connection with the stipulated judgment, SCWC and the City of Claremont entered into a water rights agreement.

6. The water rights agreement grants SCWC an exclusive lease of the city's water rights (2.772% of annual safe operating yield) at a rate set equal to 90% of the replacement water rate in effect each year for the Six Basins.

7. SCWC proposes to reduce the quantity rate applicable to the City of Claremont from \$1.475 to \$0.738 per hundred cubic feet.

8. Because of the reduction in the quantity rate, the City of Claremont will save an estimated \$109,000 in its first year under the new rate.

9. Under the water rights agreement, SCWC is granted an easement, at no charge, to drill up to five water wells on city-owned property.

10. The City of Claremont holds arguably superior overlying rights to Six Basins water.

11. As part of the agreement with SCWC, the City of Claremont would agree to cap its right to Six Basins water at 2.772% and would lease that right to SCWC for 30 years at a rate 10% less than the rate set for replacement water.

12. The Ratepayer Representation Branch opposes the application on grounds that the agreement with the city unreasonably shifts revenue requirements from the city to other ratepayers without quantifiable corresponding benefits.

### **Conclusions of Law**

1. SCWC seeks Commission approval of its participation in the stipulated judgment and the water rights agreement with the City of Claremont, pursuant to Pub. Util. Code §§ 454 and 851.

2. The stipulated judgment and the water rights agreement will provide significant benefits to SCWC and its ratepayers, both in the preservation of the Six Basins water supply and in cost avoidance for the company's sources of water in the future.

3. SCWC should be required to amend or otherwise modify its agreement with the City of Claremont to provide that if the Water Rights Agreement is terminated, and if SCWC is operating wells on city-granted easements, SCWC will pay a one-time sum of \$25,000 in 1999 dollars, escalated annually by the non-labor CPI factor determined by the Commission's ORA Monopoly Regulation Branch to the Water Division, per utilized easement to maintain the easement for the remaining useful life of the wells, based on an estimated useful life of 50 years for each well.

4. SCWC should be directed to file a tariff incorporating the approved discount in Schedule CM-7ML and incorporating the currently effective restrictions on use of irrigation water during off-peak periods.

5. The application should be approved.

6. This order should be made effective immediately so that SCWC can begin receiving the benefits of the stipulated judgment and the water rights agreement.

## **O R D E R**

### **IT IS ORDERED that:**

1. The Stipulated Judgment attached to the application as Appendix B is just and reasonable and in the public interest.

2. Southern California Water Company (SCWC) is authorized to enter into the Stipulated Judgment attached to the application as Appendix B.

3. The Water Rights Agreement attached to the application as Appendix C is just and reasonable and in the public interest.

4. SCWC is authorized to enter into the Water Rights Agreement, attached to the application as Appendix C.

5. SCWC is directed to amend or otherwise modify its agreement with the City of Claremont to provide that if the Water Rights Agreement is terminated, and if SCWC is operating wells on city-granted easements, SCWC will pay a one-time sum of \$25,000 in 1999 dollars, escalated annually by the non-labor CPI factor determined by the Commission's ORA Monopoly Regulation Branch to the Water Division, per utilized easement to maintain the easement for the remaining useful life of the wells, based on an estimated useful life of 50 years for each well.

6. SCWC is authorized to make the changes to Schedule No. CM-7ML as described in the application; provided, however, that the tariff shall include the currently effective restrictions on use of irrigation water during off-peak periods.

7. SCWC shall notify the Director of the Commission's Water Division in writing of the actual dates of execution of the Stipulated Judgment and the Water Rights Agreement, as amended or modified, as authorized herein. A true copy of the Stipulated Judgment and the Water Rights Agreement shall be attached to the notification.

8. SCWC shall file new tariffs incorporating the changes authorized by this order.

9. SCWC shall make all books and records available for review and inspection upon Commission staff request.

10. The authority granted in this order shall expire if not exercised within 12 months after the effective date of this order.



11. Resolution ALJ 176-3008, dated January 20, 1999, is amended to categorize this proceeding as ratesetting, with a determination that hearings are required.

ALJ Walker is principal hearing officer in this proceeding.

12. Application 98-12-036 is closed.

This order is effective today.

Dated September 2, 1999, at San Francisco, California.

RICHARD A. BILAS

President

HENRY M. DUQUE

JOSIAH L. NEEPER

JOEL Z. HYATT

CARL W. WOOD

Commissioners