SETTLEMENT AGREEMENT

and

MASTER WATER SALES CONTRACT

between

THE CITY AND COUNTY OF SAN FRANCISCO

and

CERTAIN SUBURBAN PURCHASERS

in

SAN MATEO COUNTY, SANTA CLARA COUNTY
AND ALAMEDA COUNTY

TABLE OF CONTENTS

		Page
Introduction		1

ARTICLE I

PARTIES

Section 1.01	Parties	3

ARTICLE II

EFFECTIVE DATE, DISPOSITION OF ACTION, RELEASE OF PAST MONETARY CLAIMS, RESERVATION OF "CO-GRANTEE" CLAIMS AND DISMISSAL OF CLAIM RE INTRA-CITY FUND TRANSFERS

Section 2.01	Effective Date	5
Section 2.02	Disposition of the Action	6
Section 2.03	Mutual Release of Past Monetary Claims	7
Section 2.04	Reservation of "Co-Grantee" Claims Under Raker Act	8
Section 2.05	Dismissal of Claim re Intra-City Fund Transfers	8

ARTICLE III

TERM

Section 3.01	Term	9
Section 3.02	Extension of Term	9
Section 3.03	Modifications During Term	9
Section 3.04	Deferral of Agreement's Term	10

ARTICLE IV

SUBURBAN REVENUE REQUIREMENT

Section 4.01	Scope of Article	11
Section 4.02	General Principles of Cost Allocation	11
Section 4.03	Operating and Maintenance Expenses	11
Section 4.04	Administrative and General Expenses	13
Section 4.05	Property Taxes	16
Section 4.06	Return on SFWD Rate Base	16
Section 4.07	SFWD Depreciation	19
Section 4.08	Suburban Hetch Hetchy Assessment	19

ARTICLE V

INTEGRATION OF SUBURBAN REVENUE REQUIREMENT WITH SFWD BUDGET DEVELOPMENT AND RATE ADJUSTMENTS

Section 5.01	General Purpose	25
Section 5.02	Budget Development	25
Section 5.03	Rate Adjustments	26
Section 5.04	Rate Structure	28
Section 5.05	Waiver and Reservation re Methodology for Determining Suburban Revenue Requirement	28
Section 5.06	Exclusions from Rate-Making Procedures	29
Section 5.07	Balancing Account	30

ARTICLE VI

ACCOUNTING PROCEDURES; COMPLIANCE AUDIT

		Page
Section 6.01	City Accounting Practices	35
Section 6.02	Calculation of Suburban Revenue Requirement	36
Section 6.03	Appointment of Independent Auditor	37
Section 6.04	Conduct of Compliance Audit	37
Section 6.05	Issuance of Auditor's Report	39
Section 6.06	Suburban Review	40

ARTICLE VII

WATER SUPPLY

Section 7.01	Supply Assurance	41
Section 7.02	Allocation of Supply Assurance	41
Section 7.03	Shortages	44
Section 7.04	Reservation of Claims to Additional Water; Service Area Expansion	45
Section 7.05	Restrictions on Resale	46
Section 7.06	Prohibition of Assignment	46
Section 7.07	Prohibition of Water Purchases from Others; Use of Local Sources; Minimum Annual Purchases; Adjustment of Service Areas	46

ARTICLE VIII

OTHER AGREEMENTS OF THE PARTIES

Section 8.01	Pricing of Additional Water	49
Section 8.02	Arbitration and Judicial Review	49
Section 8.03	Special Provisions re Attorneys' Fees	52
Section 8.04	Suburban Advisory Group	53
Section 8.05	Notice of Water Rights Proceedings	54
Section 8.06	Notice	54
Section 8.07	Rates Applicable to Other Resale Users	55
Section 8.08	Changes in the City's Water Delivery System	55
Section 8.09	Representations During Settlement Negotiations	56
Section 8.10	Counterparts	56
Section 8.11	SFWD Rules and Regulations	56
Section 8.12	Preservation of Water Rights	56
Section 8.13	Suburban Representatives	56
Section 8.14	Reservation of Claims Regarding Suburban Purchase of Water from In-City Retail Distribution System	57
Section 8.15	Expenses Chargeable to Individual Suburban Purchasers	57
Section 8.16	Incorporation of Exhibits	57
Section 8.17	Actions and Approvals by the City	57
Section 8.18	Filing of Notices	58
Section 8.19	Section Headings	58

ARTICLE IX

IMPLEMENTATION AND SPECIAL PROVISIONS AFFECTING CERTAIN SUBURBAN PURCHASERS

		Page
Section 9.01	General	59
Section 9.02	California Water Service Company	59
Section 9.03	City of San Jose and City of Santa Clara	60
Section 9.04	City of Hayward	62
Section 9.05	Estero Municipal Improvement District	62
Section 9.06	Alameda County Water District	62
Section 9.07	Dimond Public Utility District/City of Daly City	63
Section 9.08	Coastside County Water District	63
Section 9.09	Stanford University	63
Section 9.10	City of Brisbane, Guadalupe Valley Municipal Improvement District, Town of Hillsborough	64

SETTLEMENT AGREEMENT
AND MASTER WATER SALES CONTRACT

The purpose of this Settlement Agreement and Master Water Sales Contract ("Agreement") is to memorialize the understanding which the City and County of San Francisco ("the City") and certain of its suburban water purchasers have reached regarding the settlement of that certain civil action ("the action") entitled *City of Palo Alto, et al. v. City and County of San Francisco,* presently pending in the United States District Court for the Northern District of California as No. C 74 1997 RHS. This Agreement is also intended to serve as the document governing the rights and obligations of the City and these and certain other suburban water purchasers as a group, and shall be incorporated by reference into individual water supply contracts ("the Individual Contracts") between the City and each such purchaser.

The action was originally instituted in 1974, when a Complaint for Injunction and Declaratory Relief was filed, together with a Motion for Preliminary Injunction and Temporary Restraining Order. The precipitating event which caused the filing of the Complaint was the decision by the City to increase suburban water rates 20.5% while increasing in-City rates 14.5%. Plaintiffs successfully obtained a preliminary injunction barring this rate increase, which was affirmed on appeal in 1977. *City of Palo Alto v. City and County of San Francisco,* 548 F.2d 1375 (9th Cir. 1977). In 1976, Plaintiffs obtained another preliminary injunction against the City, barring the City from instituting a certain "lifeline" rate, the effect of which was disproportionately to lower rates to in-City water users.

In 1978, Plaintiffs filed an Amended and Supplemental Complaint in the action. While the prior Complaint and Motions for Preliminary Injunction had been directed specifically against certain impending rate increases, the Amended and Supplemental Complaint substantially broadened the scope of the action into an attack upon the historic method by which the City has charged suburban cities and other public entities for water. The Amended and Supplemental Complaint charged that the City's long-standing rate-setting practices violated the Raker Act, 38 Stat. 242 (1913) (hereinafter sometimes referred to as "the Act"), in a number of different respects. The Complaint sought declaratory relief regarding the rights and obligations of Plaintiffs and the City under the Act, an injunction prohibiting the City from charging unreasonable, arbitrary or discriminatory rates, and restitution by the City to Plaintiffs of any amounts charged them for water found to be in violation of the Act.

Throughout the action, the City has denied that Plaintiffs are entitled to any relief and contended that: (a) the Raker Act affords Plaintiffs no private right of action; (b) the Raker Act does not require that the City sell water to Plaintiffs at cost, but merely that the City's water rates conform to state law; and (c) the rates charged the suburban purchasers for water have been and continue to be legal under state and federal law. The City has filed a Motion for Summary Judgment based upon the first two of these claims, which is presently pending before the District Court.

During the course of the action, the parties have engaged in extensive settlement negotiations in an effort to resolve their outstanding differences amicably and provide a new framework for their future relationship. This Agreement is the product of those negotiations, and reflects the understandings which the parties hereto have reached in their efforts to settle the action. As will also be seen hereafter, this Agreement provides that certain issues as to which the parties possess conflicting views will not be resolved by this Agreement, and this Agreement shall not be construed as a concession by any signatory thereto as to any such specifically reserved issue.

The terms of the Agreement reached between the parties are as follows:

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ARTICLE I

PARTIES

Section 1.01. *Parties.*

The parties to this Agreement are the City and County of San Francisco and such of the following entities (all of whom purchase water from the City) as have executed this Agreement:

(a) The City of Palo Alto, City of Redwood City, City of Burlingame, City of Menlo Park, City of Hayward, City of San Bruno, City of Daly City, Alameda County Water District, Coastside County Water District, North Coast County Water District, Belmont County Water District, Skyline County Water District, Purissima Hills Water District, East Palo Alto County Waterworks District and the San Mateo County Waterworks District No. 3, all of whom shall hereafter collectively be referred to as "Plaintiffs";

(b) The Estero Municipal Improvement District, Town of Hillsborough, City of Millbrae, Westborough County Water District, City of Brisbane, Guadalupe Valley Municipal Improvement District, Los Trancos County Water District, City of Sunnyvale, Cordilleras Mutual Water Association, The Board of Trustees of The Leland Stanford Junior University ("Stanford University"), City of Mountain View, City of Milpitas, City of Santa Clara, City of San Jose, and the California Water Service Company.

The entities listed above in groups (a) and (b) which have executed this Agreement shall collectively be referred to as the "suburban purchasers".

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ARTICLE II

EFFECTIVE DATE, DISPOSITION OF ACTION, RELEASE OF PAST MONETARY CLAIMS, RESERVATION OF "CO-GRANTEE" CLAIMS AND DISMISSAL OF CLAIM RE INTRA-CITY FUND TRANSFERS

Section 2.01. *Effective Date.*

Except as hereinafter provided, this Agreement shall become effective only when it has been duly approved by the City and by each of the entities listed in Section 1.01(a) and (b) ("listed entities") and when the City and each of these listed entities (except for the City of Hayward and the Estero Municipal Improvement District) have entered into an Individual Contract, as provided in Section 9.01. If the City and all listed entities approve this Agreement and (except for the City of Hayward and the Estero Municipal Improvement District) an Individual Contract by May 25, 1984, the effective date shall be May 25, 1984.

If, by May 25, 1984, this Agreement has been approved by fewer than all of the listed entities and/or fewer than all of the listed entities have entered into Individual Contracts with the City, then the effectiveness of this Agreement shall be determined as follows:

(a) If suburban purchasers representing at least 80 percent in number (24) and 80 percent of the quantity of water purchased from the City by all the listed entities in calendar year 1981 (57,947,464 ccf) have approved this Agreement and (if required) their Individual Contracts, then the City shall have the option to waive its right under this section to require that all listed entities have approved this Agreement and an Individual Contract as a condition precedent to this Agreement and any Individual Contract becoming effective. The City shall have 20 days from May 25, 1984 within which to elect to waive the condition and to send notice to the listed entities which have approved this Agreement of its waiver. If the City elects to waive the condition, then those listed entities which have approved this Agreement and Individual Contracts shall be bound thereby and this Agreement and the Individual Contracts shall become effective, as of the date of the City's election, as to them. For purposes of determining whether the suburban purchasers which have approved this Agreement represent 80 percent or more of the water purchased during 1981 (i.e., 57,947,464 ccf or more), the quantity of water attributable to each listed entity shall be as set forth in Exhibit K-2.

(b) If listed entities representing less than 80 percent in number and quantity of water purchased have approved this Agreement and (if required) their Individual Contracts, then both the City and those listed entities which have signed this Agreement and Individual Contracts shall have the option to waive its and their rights under this Section to require that all listed entites have approved this Agreement and an Individual Contract as a condition precedent to this Agreement and any Individual Contract becoming effective. This option shall be exercised in the following manner. First, the City shall send notice, on or before June 1, 1984, to each listed entity which has approved this Agreement and an Individual Contract on or before May 25, 1984 of the names of all of the listed entities which have also approved this Agreement and an Individual Contract. Second, each of the listed entities which has approved this Agreement and an Individual Contract on or before May 25, 1984 shall notify the City of its decision to waive the condition by June 22, 1984. Third, if the City then elects to waive the condition, it shall notify each listed entity which has signed this Agreement and an Individual Contract of its election no later than August 7, 1984, and this Agreement and the Individual Contracts shall then become effective as to each listed entity which has elected to waive the condition, as of August 7, 1984.

(c) Notwithstanding anything in Sections 2.01(a) and (b) to the contrary, this Agreement shall not become effective unless signed by each and every Plaintiff, except as provided herein:

(1) If all Plaintiffs sign the Stipulation for Dismissal with Prejudice provided for in Section 2.02 by May 25, 1984, then the City may waive this condition by giving written notice of waiver to each listed entity no later than August 7, 1984. If this condition is thus waived,

then the effectiveness of this Agreement shall be determined under Section 2.01(a) or (b), whichever is applicable.

(2) If any Plaintiff has not signed the Stipulation for Dismissal with Prejudice provided for in Section 2.02 by May 25, 1984, then both the City and those listed entities which have signed this Agreement and an Individual Contract shall have the option to waive this condition. The option shall be exercised in the same manner as that specified in Section 2.01(b), *mutatis mutandis.* If this condition is waived pursuant to this subsection, then the effectiveness of this Agreement shall be determined under Section 2.01(a) or (b), whichever is applicable.

(d) If this Agreement becomes effective pursuant to either Section 2.01(a) or 2.01(b), then the Supply Assurance defined in Section 7.01 shall be reduced by the amount of the individual supply guarantees, set out in Exhibit K-1, of those listed entities which are not parties to the Agreement. (If the City of Hayward ("Hayward") does not become a party to this Agreement, the Supply Assurance shall be reduced by 14.53 mgd as of July 1, 1984 and shall be further reduced at three year intervals thereafter (e.g., as of July 1, 1987, July 1, 1990, etc.) by the average amount of water delivered annually by the City to Hayward in excess of 14.53 mgd during the three year period. If the Estero Municipal Improvement District ("Estero") does not become a party to this Agreement, the Supply Assurance shall be reduced by 3.95 mgd as of July 1, 1984 and shall be further reduced at three year intervals thereafter by the average amount of water delivered annually by the City to Estero in excess of 3.95 mgd during the three year period.) Corresponding reductions shall also be made in the "ultimate base rates" and in the calculation of ultimate maximum day and ultimate maximum hour rates, as defined in Exhibit J.

The parties intend that the adjustments to the Supply Assurance provided for in this subsection be made in conjunction with the adjustments required by Section 7.02(b). At such time as annual adjustments are required by Section 7.02(b)(5), the reductions in the Supply Assurance provided for herein shall also be made annually rather than triennially.

Only those listed entities which are signatories to this Agreement and an Individual Contract shall be entitled to share in "residual water" as defined in Section 7.02.

(e) No provision of Article IX which applies to fewer than all of the suburban purchasers shall become effective unless the City and the suburban purchaser(s) to which the provision refers sign this Agreement and (except for Hayward and Estero) their Individual Contracts.

(f) The time limits in subsections (a), (b) and (c) of this Section may be extended by agreement of counsel for the City and Plaintiffs, for a period not to exceed sixty (60) days.

Section 2.02. *Disposition of the Action.*

At the time each of the Plaintiffs signs the Agreement and (except the City of Hayward) an Individual Contract, each Plaintiff also shall sign a Stipulation for Dismissal with Prejudice of the action ("the Stipulation") in the form attached hereto as Exhibit N. If all Plaintiffs sign the Stipulation, or if the City and those listed entities which have signed this Agreement and an Individual Contract exercise the option provided in Section 2.01(c)(2), then forty days after the last of the notices provided for in Section 8.18 has been filed, the City is authorized to and shall file the Stipulation on behalf of it and all Plaintiffs which have signed the Stipulation with the Clerk of the United States District Court for the Northern District of California.

The Stipulation shall recite that the prior injunctions entered in the action shall be vacated. Each party shall bear its own costs, including attorneys' fees, incident to its participation in the action.

In the event that a final judgment is entered by a court of competent jurisdiction declaring this Agreement to be invalid, the Stipulation shall not bar a listed entity from filing the same or a sim-

ilar action as the action which is dismissed by the Stipulation, except that a listed entity which joins in or supports a judicial challenge which results in the judgment declaring the Agreement to be invalid shall be barred from filing the same or a similar action as that dismissed by the Stipulation. By signing this Agreement, each party hereto explicitly and knowingly waives any and all rights to commence or maintain any action or proceeding to challenge its validity.

Each entity listed in subsection 1.01(b) which becomes a signatory to this Agreement hereby agrees that the Stipulation shall have the same force and effect as applied to it that the Stipulation has with respect to the Plaintiffs which sign it and that any claim the assertion of which would be barred by the Stipulation with respect to a Plaintiff signatory shall similarly be barred if asserted by a non-Plaintiff signatory of this Agreement.

Section 2.03. *Mutual Release of Past Monetary Claims.*

In the action, Plaintiffs asserted, *inter alia*, monetary claims against the City based on alleged historical overcharges for water sold by the City to suburban purchasers. The City in the action contended, *inter alia*, that it had historically undercharged suburban purchasers for water. The parties to this Agreement desire to release each other from any liability on account of such claimed monetary overcharges or undercharges, as follows:

(a) Each listed entity which is a signatory hereto releases City of and from any and all monetary claims for overcharges arising out of sales of water by City to such entity prior to June 30, 1984. This release shall not extend to any contested water billing between City and such entity, heretofore existing or hereafter arising, on grounds unrelated to the issues raised in the action, such as (without limitation) errors in billing, errors in the rate schedule applied, and disputes over the amount of water sold during a billing period; however, each such entity hereby warrants and represents to City that it knows of no such unrelated claims as of thirty days before the date of its signature hereto which have not been disclosed to the City. This release shall include all monetary claims for overcharges on water sold by the City prior to June 30, 1984, which were raised in the action or which could have been raised in the action, whether based on federal law (including the Raker Act), state law, the Charter of the City and County of San Francisco, or any other applicable provision of law.

(b) The City releases each listed entity which is a signatory hereto of and from any and all monetary claims for undercharges arising out of sales of water by the City to such entity prior to June 30, 1984. This release shall not extend to any contested water billing between the City and such entity, heretofore existing or hereafter arising, on grounds unrelated to the issues raised in the action, such as (without limitation) errors in billing, errors in the rate schedule applied, and disputes over the amount of water sold during a billing period; however, the City warrants and represents that it knows of no such unrelated claims against any such entity as of thirty days before the date of its signature hereto which have not been disclosed to the entity affected. This release shall include all monetary claims for undercharges on water sold prior to June 30, 1984, which were asserted by City or which could have been asserted by City in the action, whether by way of defense, counterclaim or otherwise, whether based on federal law (including the Raker Act), state law, the Charter of the City and County of San Francisco, or any other applicable provision of law.

(c) Each of the signatories to this Agreement hereby acknowledges that it is familiar with the provisions of and has been advised as to the meaning and effect of waiver of the rights and benefits conferred by California Civil Code Section 1542, and hereby knowingly waives the rights and benefits conferred by that section, which provides:

> "A general release does not extend to claims which the creditor does not know or suspect to exist in his favor at the time of executing the release, which if known by him must have materially affected his settlement with the debtor."

Section 2.04. *Reservation of "Co-Grantee" Claims Under Raker Act.*

Plaintiffs contended in the action that they and the other suburban purchasers which are municipalities or water districts are "co-grantees" within the meaning of Section 8 of the Act, and are entitled to certain rights, benefits and privileges by virtue of that status. The City has denied those claims. Nothing in this Agreement (or in the Individual Contracts which shall subsequently be entered into between the parties incorporating this Agreement) shall be construed or interpreted in any way to affect or influence the ultimate resolution of the controversy between the parties concerning whether any of the suburban purchasers are "co-grantees" under the Raker Act and, if so, what rights, benefits and privileges accrue to them by reason of that claimed status, nor shall the dismissal with prejudice filed pursuant to Section 2.02 bar the future adjudication of such claims. Notwithstanding anything in this Section, this Agreement shall determine the respective monetary rights and liabilities of the parties with respect to the water sold by the City to the suburban purchasers during the Term hereof, and such rights and liabilities shall not be affected by any judgments or orders issued by any court in any other litigation, whether or not between the parties hereto, and whether or not related to the controversy over co-grantee status, except for arbitration and/or litigation reserved by Section 8.01 or initiated pursuant to Section 8.02. The reservation of Raker Act rights in this Section is subject to the waiver of those rights in Sections 5.05(b) and 8.01(b) and (c).

Section 2.05. *Dismissal of Claim re Intra-City Fund Transfers.*

Plaintiffs contended in the action that a certain proposed transfer of funds from the San Francisco Water Department (SFWD) to the City's General Fund violated provisions of state and federal law (including the Act) as well as then-existing contracts between Plaintiffs and the City. The suburban purchasers hereby acknowledge that the filing of the Stipulation described in Section 2.02 shall dismiss with prejudice all those claims asserted in the action with respect to transfers of funds and that unless such Stipulation ceases to be a bar to the filing of the same or a subsequent action pursuant to the penultimate paragraph of Section 2.02, these claims shall be forever barred as to them. Each suburban purchaser hereby unconditionally waives and releases the City from any and all claims heretofore or hereafter arising from transfers by the City, not prohibited by its Charter, of funds from the SFWD to any other department or fund of the City, during the Term of this Agreement, and further agrees unconditionally not to contest the validity of any such transfer before any court or administrative official, tribunal or agency. However, this waiver and release shall not absolve the City from the performance of any duty or obligation imposed under this Agreement, and it shall be no defense to any proceeding, whether judicial or arbitral, brought to enforce the terms of this Agreement or for the breach thereof, that performance by the City has been rendered impossible or impracticable because of any transfers of funds from the SFWD to any other department or fund of the City. Nothing in this Section is intended or shall be construed to infringe the City's right under Section 5.03(b)(1) to raise rates on an emergency basis to cover capital expenses if the SFWD does not have sufficient unappropriated funds available for use and is unable to obtain sufficient funds, in the time necessary, through the issuance of bonds or from state or federal grants.

ARTICLE III

TERM

Section 3.01. *Term.*

The term ("Term") of this Agreement shall be twenty-five (25) years. The Term shall begin on July 1, 1984, regardless of whether the effective date is before or after that date, and shall end on June 30, 2009, provided that the City shall have no obligation to comply with the provisions of Section 5.02 and 5.03 prior to the effective date of the Agreement. Except as provided in Article IX, the Term of all Individual Contracts shall also begin on July 1, 1984 and end on June 30, 2009.

Section 3.02. *Extension of Term.*

After the expiration of the Term, this Agreement may be extended by mutual consent of the parties, subject to any modifications thereof which may be determined at that time. If fewer than all of the parties signatory hereto desire to extend this Agreement beyond its Term, with or without modifications, the City and those of the suburban purchasers who wish to extend the Agreement shall be free to do so, provided that no party to this Agreement which does not wish to become a party to such an extended Agreement shall be compelled to do so by the actions of any other party to this Agreement under this Section.

Section 3.03. *Modifications During Term.*

(a) At any time during the Term of this Agreement, or any extension thereof, the parties agree, if requested by any signatory hereto, to conduct mutual negotiations in good faith on the subject of any modifications hereof which may be desired by any signatory hereto and, pursuant to such negotiations, this Agreement may be amended by mutual consent of all parties.

(b) This Agreement may also be amended with the consent of the City and of suburban purchasers representing at least 95 percent of the quantity of water delivered by the City to all suburban purchasers during the preceding fiscal year, provided that no amendment substantially and adversely affecting a fundamental right of a suburban purchaser under this Agreement may be made without the consent of that purchaser. Fundamental rights of suburban purchasers include, but are not limited to, their status as parties to this Agreement, their allocation of water as provided in Sections 7.02 and 7.03, and any specific rights conferred in Article IX. No amendment to Article IV or Section 5.04 which has the effect of discriminating against any individual suburban purchaser or any group of fewer than all of the suburban purchasers shall become effective without the consent of the suburban purchaser(s) thereby adversely affected. Amendments to Article IV which merely affect the allocation of expenses between direct City water users, on the one hand, and the suburban purchasers collectively, on the other, and amendments to Sections 5.02, 5.03, 5.06 and 5.07(a) through (d) and Article VI which merely alter the budgetary, rate-making, balancing account, accounting and auditing procedures described therein, shall become effective if approved by the City and suburban purchasers representing at least 95 percent of the quantity of water delivered by the City to all suburban purchasers during the preceding fiscal year.

(c) When an amendment has been approved by the City and 95 percent of the suburban purchasers (as herein defined) pursuant to subsection (b), the City shall give notice of the amendment's adoption to the suburban purchasers. Notwithstanding any other provision of law or this Agreement, any suburban purchaser which claims that an amendment to this Agreement that has been approved pursuant to subsection (b) violates its rights under that subsection shall have thirty days from the date the City sends the notice of the amendment's adoption in which to challenge the amendment's validity through appropriate judicial action. If no such action is filed within said thirty day period, the amendment shall be finally and conclusively deemed to have been adopted in compliance with this Article.

(d) If this Agreement becomes effective pursuant to either Sections 2.01(a) or 2.01(b), then it may be amended to admit additional listed entities as parties, until August 7, 1984, with the consent of the City and suburban purchasers representing 66.7 percent of the 1981 water usage of those listed entities that have already become parties. After August 7, 1984, the admission of new listed entities as parties shall require 95 percent approval and the admission of new parties who are not listed entities shall require the consent of the City and all suburban purchasers.

(e) Notwithstanding the provisions of subsections (a) and (b), any provision of Article IX which applies only to an individual suburban purchaser may be amended with the concurrence of the City and the suburban purchaser to which it applies; provided that the amendment will not, directly or indirectly, adversely affect either the quantity of water available to other suburban purchasers or the cost of that water to other suburban purchasers. (An example of provisions in Article IX whose amendment is not permissible under this subsection is the maximum water delivery levels and service areas for San Jose and Santa Clara provided for in Section 9.03.)

Before making any such amendment effective, the City shall give notice, with a copy of the text of the proposed amendment, to all other suburban purchasers. The suburban purchasers shall have sixty (60) days in which to object to the amendment on the ground that it is not permissible under this subsection. If no such objection is received by the City, the proposed amendment may become effective. If one or more suburban purchasers object to the amendment, the City, the individual suburban purchaser with which the City intends to effect the amendment, and the suburban purchaser(s) which lodged the objection shall meet to discuss the matter.

If the dispute cannot be resolved and the City and the suburban purchaser involved elect to proceed with the amendment, either the City or the suburban purchaser shall give written notice of such election to each suburban purchaser which has objected. Any suburban purchaser which has objected to such amendment shall have sixty (60) days from receipt of this notice within which to commence an action challenging the validity of such amendment, and such amendment shall be deemed effective as of the end of this 60-day period unless restrained by order of court.

(f) Notwithstanding the foregoing provisions of this Section, the City may amend Exhibit J with the consent of the Suburban Representatives to reflect changes in the inputs into the SFWD wholesale system, changes in service connections, additions or retirement of assets, or any other change that would affect the calculation of the usage rates and ratios described in Exhibit J. The Suburban Representatives shall not unreasonably withhold consent to amendments proposed by the City. If the Suburban Representatives do not consent to an amendment proposed by the City, the City may implement the amendment and perform the calculations described in Exhibit J in accordance with the terms of the amendment, unless and until an arbitrator orders otherwise.

(g) Notwithstanding the foregoing provisions of this Section, the City may amend Exhibit E as provided therein, subject to the provisions concerning notice and arbitration contained therein.

Section 3.04. *Deferral of Agreement's Term.*

The Term of the Agreement referred to in Section 3.01 was originally contemplated to commence on July 1, 1983, and it now has been agreed that the Term will commence on July 1, 1984. Because of the deferral of the commencement date of the Term, the Ciy hereby agrees that: (1) there shall be no rate increases for fiscal year 1984/85 applicable to suburban purchasers, provided that this provision shall not preclude an emergency rate increase if permitted under Section 5.03(b); (2) it will not, because of the execution of this Agreement, defer to fiscal year 1984/85 the incurring or accrual of any item of operating, maintenance, or administrative and general expense which otherwise would have been incurred or accrued during fiscal year 1983/84; and (3) it will not, because of the execution of this Agreement, delay beyond June 30, 1984, the completion or placement into service of revenue-funded assets under construction in fiscal year 1983/84 which otherwise would have been completed or placed into service during said fiscal year.

ARTICLE IV

SUBURBAN REVENUE REQUIREMENT

Section 4.01. *Scope of Article.*

This Article shall be applicable only to the rates charged by the City to the suburban purchasers for water delivered pursuant hereto. Nothing contained in this Agreement (with the exception of Section 8.07) shall be interpreted or construed so as to limit, constrain or in any way affect the rates which San Francisco may charge for water sold to water users within the City's geographical boundaries, water sold to City departments or agencies located outside of the City's geographical limits, water sold to the City's other water purchasers located outside of the City's geographical limits (including those listed entities which do not execute this Agreement) or the methodology by which any or all of such rates are determined. These three categories of water users are referred to herein as "direct City water users." Suburban purchasers, as defined in Article I, and direct City water users, as defined in this Section, represent all existing users of water supplied by the San Francisco Water Department.

Section 4.02. *General Principles of Cost Allocation.*

The purpose of this Article is to set forth the method by which the suburban purchasers' collective share of the San Francisco Water Department's (SFWD's) total revenue requirements will be determined. This collective share shall be termed the "suburban revenue requirement." The suburban revenue requirement will consist of the sum of the suburban purchasers' allocated shares of the operating and capital costs, determined on the utility basis as hereinafter set forth, incurred by the SFWD in providing water to the suburban purchasers. Specifically, the suburban revenue requirement will consist of and be limited to the following six categories:

- operating and maintenance expenses
- administrative and general expenses
- property taxes
- return on rate base
- depreciation on utility plant
- the Suburban Hetch Hetchy Assessment

In each of these categories, costs related only to providing water to direct City water users ("direct City costs") will be allocated entirely to such users. Costs related only to providing water to suburban purchasers ("direct suburban costs") will be allocated entirely to such users. Costs related to providing water to both direct City water users and to suburban purchasers ("joint costs") will be allocated between the City and the suburban purchasers in accordance with the following methodology. "Wholesale" costs shall include both joint costs and direct suburban costs.

Section 4.03. *Operating and Maintenance Expenses.*

There are five categories of Operating and Maintenance expenses:

(a) *Source of Supply.*

Description: This category includes operating and maintenance expenses attributable to collecting and impounding reservoirs, lakes, tunnels, wells, and supply mains operated by the SFWD. Outside-City joint expenses in this category are presently assigned to the SFWD accounts listed in Exhibit A-1.

Allocation: Source of supply expenses attributable to operation and maintenance of components of the system benefitting only direct City water users, which are identified as in-City expenses in the SFWD cost ledgers (i.e., expenses posted to accounts beginning with "4" or "64"), will be allocated

to the City. Source of supply expenses attributable to operation and maintenance of components of the system benefitting both direct City water users and suburban purchasers, which are identified in the City's cost ledgers as outside-City expenses (i.e., expenses posted to accounts beginning with "5" or "65"), will be jointly allocated between the City and the suburban purchasers on the basis of annual proportional usage of water, i.e., at the "current base rates" as defined in Exhibit J.

(b) *Pumping.*

Description: This category includes labor, fuel and power purchased for pumping water, and the operation and maintenance of pumping equipment. Outside-City joint pumping expenses are presently assigned to the SFWD accounts listed in Exhibit A-2. (In determining pumping charges the City shall be entitled to have the Hetch Hetchy Water and Power Department (HHWPD) bill SFWD for power supplied to SFWD by HHWPD at rates which shall not exceed the rates which would be charged by the Pacific Gas & Electric Company for providing like classes of electric service under its then-current rate schedules.)

Allocation: Pumping expenses shall be allocated on the basis of the City's cost ledger location codes (in the same manner as source of supply expenses) with in-City expenses allocated entirely to the City and outside-City expenses allocated jointly between the City and the suburban purchasers. Outside-City joint pumping expenses shall be allocated at the current base rates.

(c) *Purification.*

Description: This category includes labor, purchase of supplies, and the operation and maintenance of facilities used for water treatment. Outside-City joint purification expenses are presently assigned to the SFWD accounts listed in Exhibit A-3.

Allocation: Purification expenses will be allocated on the basis of the City's cost ledger location codes (in the same manner as source of supply expenses), with in-City expenses allocated entirely to the City and outside-City expenses allocated jointly between the City and the suburban purchasers. Outside-City joint purification expenses shall be allocated at the current base rates.

(d) *Transmission and Distribution Expenses.*

Description: The wholesale portion of this category includes operating and maintenance expenses attributable to the storage and distribution reservoirs and appurtenant mains, suburban meters and services, and certain related miscellaneous expenses. Direct suburban and joint transmission and distribution expenses are presently assigned to the SFWD accounts listed in Exhibit A-4.

Allocation: Transmission and distribution expenses shall first be divided between in-City expenses and outside-City expenses on the basis of the City's cost ledger location codes (in the same manner as source of supply expenses), with in-City expenses allocated entirely to the City and outside-City expenses allocated jointly between the City and the suburban purchasers. This general rule is subject to two exceptions.

First, the transmission and distribution expenses related to Sunset Reservoir (Account No. 467760), University Mound Reservoir (Account No. 468760), and Merced Manor Reservoir (Account No. 469760) shall be allocated as outside-City joint expenses, despite their in-City categorization in the SFWD cost ledger location codes.

Second, the following outside-City expenses related to the Palo Alto Pipeline shall be allocated entirely to the suburban purchasers without further allocation:

539753	Transmission & Distribution Lines Expense
539761	Maintenance of Transmissions & Canals

After these modifications have been made, outside-City joint transmission and distribution expenses shall be allocated between the City and the suburban purchasers at the current base rates.

(e) *Customer Accounts.*

Description: This category includes meter reading, customer record keeping and collection costs. It presently consists of the line items in the SFWD cost ledgers listed in Exhibit A-5.

Allocation: Customer accounts expenses will be allocated 98% to the City and 2% to the suburban purchasers.

Section 4.04. *Administrative and General Expenses.*

Description: This category consists of expenses associated with the administration of the SFWD and other general expenses, including City overhead and the San Francisco Public Utilites Commission charges. While the majority of these expenses are identified as in-City expenses in the City's cost ledger location codes, most in fact benefit both wholesale and in-City water users. Accordingly, they are not allocated on the basis of location code identification.

There are three subcategories of Administrative and General Expenses, which are to be calculated and allocated as follows.

(a) *City Overhead.*

This subcategory consists of support services provided by the City's central service departments which have not been directly billed to SFWD or other operating departments. All operating departments of the City are assigned a prorated share of these unbilled costs, although only those City departments which are not supported by ad valorem taxes actually reimburse the City's general fund for their share. The SFWD's share of these costs is presently identified in the SFWD cost ledgers as Account No. 649000-0920.

The parties have agreed in principle that the bases on which these costs are allocated to the SFPUC, the SFWD and the HHWPD should fairly reflect the proportional benefit which each receives (along with other City departments and agencies) from the central service department whose costs are being allocated. The parties have also agreed that costs of central service departments allocated by the City in accordance with a "Countywide Cost Allocation Plan" ("COWCAP") prepared annually by the City and submitted to and approved by the Bureau of Cost Plans in the State Controller's office (or its successor) should be entitled to a rebuttable presumption that they have been fairly allocated for purposes of this Agreement. However, the parties have not been able to agree on specific limits or allocational bases for costs of central service departments not reimbursable by the federal government and hence not included in the annual COWCAP. Accordingly, for purposes of this Agreement, City overhead allocable to direct City water users and suburban purchasers shall be determined in the following manner.

For FY 1984/85, the City overhead charge shall be deemed to equal $600,000 for the SFWD and $240,000 for the SFPUC. For the next four succeeding fiscal years (e.g., FY 1985/86 through 1988/89), the City overhead charge shall be deemed to equal the deemed City overhead charge for FY 1984/85, adjusted to reflect changes in the San Francisco-Oakland Metropolitan Area Consumer Price Index (All Urban Consumers, 1967=100). (This index level is 307.3 as of December 1983.) The index level as of June 1984 shall be the Base Index. The deemed City overhead charge for (e.g., FY 1985/86) shall be adjusted based on the percentage change from the Base Index to the index as of June 1985. The deemed City overhead charge as so computed shall be in lieu of all other City overhead charges whether or not included in the annual COWCAP. In addition, the deemed City overhead charge will be reduced if costs of central service departments included in the COWCAP prepared for FY 1983/84 and certified by the City's Controller on February 18, 1983 are thereafter billed directly to the operating departments rather than allocated, via COWCAP or otherwise, and increased if costs of central service departments directly billed to the operating departments as of FY 1983/84 are thereafter allocated to the SFWD, via COWCAP or otherwise, rather than billed directly.

Before the close of fiscal year 1988/89, the City and the Suburban Representatives shall meet to discuss how City overhead shall be allocated to the suburban purchasers in fiscal years after FY 1988/89. As the result of these negotiations, the City and the Suburban Representatives may agree either on a methodology for actually allocating City overhead to the SFWD, the SFPUC and the HHWPD or, in the alternative, on a procedure for determining a "deemed City overhead charge" (such as that described in the preceding paragraph for FY 1984/85 through 1988/89) to be annually substituted for purposes of this Agreement for the actual City overhead annually charged to the SFWD, the SFPUC and the HHWPD.

If the City and the Suburban Representatives are unable to reach either of the agreements specified in the preceding paragraph after negotiations, the City or any of the suburban purchasers may invoke arbitration pursuant to Section 8.02. The arbitrator shall have no power to direct the City's actual allocation of City overhead to the SFWD, the SFPUC, or the HHWPD, but shall have power to specify a "deemed City overhead charge" (or procedure for determining such charge) which fairly allocates the costs of central service departments in accordance with the principle set forth above. The "deemed City overhead charge" specified by the arbitrator or determined through the procedure specified by the arbitrator shall then be annually substituted for the actual City overhead annually charged to the SFWD, the SFPUC and the HHWPD. No "deemed City overhead charge" nor procedure specified by an arbitrator for determining the annual "deemed City overhead charge" shall last longer than five fiscal years. During the last year of that period, the City and the Suburban Representatives shall again attempt to negotiate an agreement in accordance with the preceding paragraphs. If these negotiations are unsuccessful, the matter will be referred to arbitration again for the determination of another "deemed City overhead charge" or procedure for determining such charge to be used during the next succeeding five-year period.

(b) *San Francisco Public Utilities Commission Charges.*

This subcategory consists of support services provided by the San Francisco Public Utilities Commission (SFPUC) and its constituent bureaus to the SFWD and the other operating departments under the jurisdiction of the SFPUC. It is presently identified in the SFWD cost ledgers as Accounts No. 649014 and 649000-3600.

The bases by which these costs are allocated among the operating departments shall fairly reflect the proportional benefit which each department receives from the SFPUC support services and bureaus whose costs are being allocated.

In order to implement the foregoing principle, the City will allocate those costs of SFPUC support services and bureaus which are reimbursable by the federal government under federal grant guidelines (hereafter called "federally allowable PUC costs") in accordance with the allocational bases included in the annual "PUC Indirect Cost Allocation Plan" for the fiscal year in question prepared by the City and submitted to the Division of Cost Allocation of the United States Department of Health and Human Services, or its successor, provided that the costs of leasing SFWD revenue-producing properties, now accounted for in the Real Estate Department within the Bureau of Administration, shall not be allocated to the suburban purchasers.

Costs of SFPUC support services and bureaus allocated in accordance with the allocational bases prescribed for them in a "PUC Indirect Cost Allocation Plan" submitted by the City to the Division of Cost Allocation of the United States Department of Health and Human Services and approved by said Division (or its successor) shall (with the exception of the leasing costs noted above) be entitled to a rebuttable presumption that they have been fairly allocated for purposes of this Agreement.

Costs of SFPUC support services and bureaus which are not reimbursable by the federal government under federal grant guidelines (i.e., which are not federally allowable PUC costs) may

nevertheless be allocated to the suburban purchasers. Such costs shall be allocated to the SFWD on the bases set out in Exhibit A-6.

The allocational bases set out in Exhibit A-6 may be changed by the City to correspond with changes in the allocational bases for federally allowable SFPUC costs which are approved or required by the federal government (or its delegate), to reflect changes in organization within the SFPUC or its departments, or changes in the functions performed by the departments whose costs are being allocated, or to increase the accuracy and/or equity of the SFPUC cost allocation process. Any changed allocational bases must similarly comply with the principle stated above.

The City overhead costs allocated to the SFPUC under the Countywide Cost Allocation Plan (COWCAP) described in paragraph (a) above, or other allocational procedure, shall not be charged to the suburban purchasers since those costs are to be replaced by the "deemed City overhead charge" determined under that paragraph. The deemed City overhead charge so determined shall, however, be allocated among MUNI, SFWD and HHWPD in the same proportion that the COWCAP costs allocated to the SFPUC are reallocated to the operating departments by the PUC Indirect Cost Allocation Plan for each fiscal year. This allocation of the deemed City overhead charge shall be entitled to the same rebuttable presumption described above for other costs so allocated.

(c) *Other.*

The remaining administrative and general expenses which are partially allocable to the suburban purchasers presently consist of the line items in the SFWD cost ledgers listed on Exhibit A-7; provided that the maximum amount which may be allocated in any year to the suburban purchasers as the result of payments by the City for claims arising out of breaks occurring in water transmission lines and mains and in-City reservoirs which are not included in the SFWD wholesale utility plant shall be $100,000. Claims expenses covered by this annual aggregate limitation are presently identified in the SFWD cost ledgers as Account No. 649031. The $100,000 limitation shall be automatically adjusted every year in accordance with changes in the Consumer Price Index for the San Francisco-Oakland Metropolitan Area, provided that in no event will it be reduced below $100,000.

Allocation: Except as provided in the following paragraph, City overhead, SFPUC charges, and other administrative and general expenses shall be allocated between the City and the suburban purchasers on the basis of the composite of the allocated expenses in the five Operating and Maintenance categories. The suburban share of these expenses shall be equal to the total of such expenses (determined as set out above) times the following fraction:

$$\frac{\text{Suburban share of SFWD source of supply, pumping, transmission and distribution, purification, and customer accounts expenses}}{\text{Total SFWD source of supply, pumping, transmission and distribution, purification, and customer accounts expenses}}$$

Administrative and general costs incurred by the SFPUC and SFWD in connection with the implementation and administration of this Agreement (which are presently assigned to Account No. 649024) shall be allocated equally between the City and the suburban purchasers. The intent of this paragraph is that the expense of new operations and procedures incurred as a result of the City's obligations under this Agreement (including but not limited to preparation of the estimated suburban revenue requirement under Section 5.03 and the interim and final suburban revenue requirements under Section 6.02) will be allocated equally to the City and the suburban purchasers but that expenses associated with administrative operations and procedures which existed prior to the effective date of this Agreement or which are not incurred as a result of the City's obligations under this Agreement will be allocated as provided above and will not be transferred to this account.

Expenses in this account in excess of $200,000 in any fiscal year shall be allocated pursuant to the formula in the preceding paragraph. Costs of the compliance audit allocated to the City under Section 6.03(b) and costs allocated to the City under Section 6.06 regarding the Suburban Review shall not be chargeable against this $200,000 limit. This $200,000 limit shall be automatically adjusted every year in accordance with changes in the Consumer Price Index for the San Francisco-Oakland Metropolitan Area, provided that in no event will it be reduced below $200,000.

Section 4.05. *Property Taxes.*

Description: This category consists of ad valorem property taxes levied against SFWD properties located in San Mateo, Santa Clara and Alameda Counties. It presently consists of the costs recorded in Account No. 659019 in the SFWD cost ledgers.

Allocation: All property tax expenses will be allocated between the City and the suburban purchasers at current base rates; provided, however, that the total property taxes allocable will first be reduced by the amount of said taxes which are passed through to tenants or users of SFWD property and reimbursed to the City by such tenants or users.

Section 4.06. *Return on SFWD Rate Base.*

(a) *Description:* Return on the SFWD rate base consists of the SFWD's return on that portion of its wholesale net utility plant and wholesale working capital allowance allocable to the suburban purchasers. The return on the SFWD rate base is the product of (1) the portion of the total SFWD rate base allocable to the suburban purchasers times (2) the overall rate of return. Each component shall be calculated as set forth below.

(b) *Calculation of Rate Base.*

The portion of the total SFWD rate base on which a return is to be paid is the suburban purchasers' share of the wholesale rate base. The wholesale portion of the total SFWD rate base must first be determined. Thereafter, the wholesale rate base must be allocated between the City and the suburban purchasers.

(i) *SFWD Wholesale Rate Base.*

The wholesale portion of the total SFWD rate base shall be the sum of (1) the average of the wholesale portion of SFWD net utility plant in service at the beginning of the year and the wholesale portion of SFWD net utility plant in service at the end of the year (i.e., the beginning wholesale net utility plant plus capital additions less depreciation, retirements and other dispositions removing an asset from utility plant in service) and (2) a wholesale working capital allowance (calculated as shown in Exhibit B-3) equal to one-sixth (⅙) of the annual wholesale SFWD operating and maintenance expenses and wholesale SFWD administrative and general expenses. As used in the previous sentence, "wholesale SFWD administrative and general expenses" shall be equal to the product of total SFWD administrative and general expenses times the following fraction:

$$\frac{\text{Wholesale SFWD source of supply, pumping, purification, transmission and distribution, and customer-accounts expenses}}{\text{Total SFWD source of supply, pumping, purification, transmission and distribution, and customer-accounts expenses}}$$

(For purposes of computing this ratio, wholesale customer accounts expense shall be deemed to be two (2) percent of total customer accounts expense.)

The wholesale portion of the SFWD net utility plant in service shall be the sum of the net book values, determined on the basis of depreciated original cost, of (1) all bond-funded SFWD

assets or portions thereof except those used to serve only direct City water users, as defined above, included in net utility plant as of June 30, 1984; and (2) all assets or portions thereof, however funded, added to net utility plant in service after June 30, 1984 except: (a) assets used to serve only direct City water users; and (b) assets, or portions thereof, funded from federal or state grants or direct user contributions. Thus, assets added to utility plant during fiscal year 1983/84 and funded from revenue shall not be included in the wholesale rate base for purposes of this Agreement. (A list of the revenue-funded assets which the City expects to add to the SFWD utility plant during fiscal year 1983/84 is shown in Exhibit B-4; these assets will not be included in the SFWD wholesale rate base for purposes of this Agreement regardless of whether they are actually placed into service during FY 1983/84 or thereafter.)

If the City finances the acquisition of new assets for the SFWD by means other than from revenues or through bonded debt (e.g., by means of leases), the capitalization of those assets, the treatment of related expenses and related debt, and all other aspects of their accounting treatment, for purposes of this Agreement, shall be in accordance with Generally Accepted Accounting Principles, as amended from time to time.

The net book value of all debt-funded assets included in net utility plant in service as of June 30, 1983 and their categorization as direct City, direct suburban or joint (which includes the eight subcategories of joint equipment assets described below) is shown in Exhibit B. The City will furnish the Suburban Representatives a list of all debt funded assets, together with the asset number, category, net book value, service life and annual depreciation for each, added to the SFWD utility plant during FY 1983/84. This list shall be delivered on or before December 31, 1984.

Interest on new debt-funded assets shall be capitalized in accordance with applicable Generally Accepted Accounting Principles, as amended from time to time.

(ii) *Suburban Share of SFWD Wholesale Rate Base.*

The suburban purchasers' share of the SFWD wholesale rate base shall consist of (1) a share of the wholesale working capital allowance defined above and (2) a share of the SFWD wholesale net utility plant in service.

The suburban purchasers' share of the wholesale working capital allowance is equal to one-sixth (1/6) of their share of wholesale SFWD operating and maintenance and administrative and general expenses, as determined pursuant to Sections 4.03 and 4.04 and as illustrated in Exhibit B-3.

The suburban purchasers' share of the SFWD wholesale net utility plant in service shall be the sum of the suburban share of each asset included therein. Each asset in the SFWD wholesale net utility plant shall be assigned to a category, based upon its characterization, and each category will be allocated between the City and suburban purchasers based on their respective use of assets within that category. The categories into which the assets in the SFWD wholesale net utility plant are segregated are as follows:

Land

Direct suburban

Joint

Equipment

Direct suburban

Joint

Joint equipment assets are further subdivided ino the following subcategories:

Current base

Ultimate base

Current maximum day

Ultimate maximum day

Current maximum hour

Ultimate maximum hour

Standby

Composite

The definitions of each of these categories and subcategories and the allocational basis or formula by which each is to be allocated between the City and the suburban purchasers are contained in Exhibit C. The categorization of each asset included in the SFWD net utility plant in service as of June 30, 1983 is listed in Exhibits B-1 and B-2. The categorization of assets (and thus their subsequent allocation) added to the SFWD net utility plant in service after June 30, 1983 shall be as agreed upon by the parties and, in the event they are unable to agree, by arbitration as provided in Section 8.02. Debt funded assets scheduled to be added during FY 1983/84 shall be categorized as shown in Exhibit B-5.

(c) *Calculation of Overall Rate of Return.*

The overall rate of return on the SFWD wholesale rate base is equal to the sum of (1) the product of the cost of SFWD wholesale debt times the SFWD wholesale debt percentage and (2) the product of the return on SFWD wholesale equity times the SFWD wholesale equity percentage.

Each of these terms shall be defined and/or derived as follows:

(i) The cost of SFWD wholesale debt is the wholesale debt interest expense for the year divided by the average outstanding balance of SFWD wholesale debt. At any given date, SFWD wholesale debt outstanding is that portion of total SFWD debt outstanding the proceeds of which have been used to finance the construction or acquisition of assets included in the SFWD wholesale utility plant in service as of that date. The average outstanding balance of SFWD wholesale debt is the beginning of the year balance plus the end of the year balance, divided by 2. The cost of SFWD wholesale debt for FY 1983/84 is estimated to be 5.1355%, as shown in Exhibit D-1.

(ii) The SFWD wholesale debt percentage is the percentage obtained by dividing the average outstanding balance of SFWD wholesale debt by the sum of (a) the average SFWD wholesale net utility plant in service plus (b) the wholesale working capital allowance defined in Section 4.06(b)(i).

The SFWD wholesale debt percentage for FY 1983/84 is estimated to be 26.16%. In subsequent years, SFWD wholesale debt shall include all outstanding City debt, the proceeds of which are used to construct or acquire SFWD wholesale assets. The wholesale portion of any debt issued in the future, some or all of which is used to construct or acquire SFWD assets, will be equal to a fraction, the numerator of which shall be the original cost of wholesale utility plant assets financed by the proceeds of such debt, and the denominator of which shall be the total proceeds of such debt.

The wholesale share of currently outstanding debt shall be as shown in Exhibit D-1.

(iii) The return on SFWD wholesale equity shall be calculated by determining the arithmetic average of the rates of return authorized by the California Public Utilities Commission (CPUC) on common equity for Class A water utilities during the last full calendar year immediately preceding the fiscal year for which the SFWD rate is to be developed. All water utilities presently

classified as Class A by the CPUC are listed on Exhibit E. In determining the average rate of return authorized by the CPUC, decisions authorizing the same rate of return on common equity to different districts or divisions of the same utility will be counted as one decision. The CPUC average rate of return shall then be multiplied by 85% to determine the rate of return on SFWD wholesale equity.

(iv) The SFWD wholesale equity percentage is equal to 100% minus the SFWD wholesale debt percentage.

The methodology for calculating the overall rate of return on SFWD wholesale rate base is shown on Exhibit F-1.

Section 4.07. *SFWD Depreciation.*

SFWD depreciation is the annual depreciation expense on the original cost of assets in the wholesale portion of SFWD utility plant in service. The "original cost" of each asset used for calculating depreciation for purposes of this Agreement shall be equal to the original cost of the asset minus any revenue-funded portions thereof (including capitalized interest funded from revenue) added to the rate base prior to June 30, 1984 and any portion of the asset financed from federal or state grants or direct user contributions.

The original cost, salvage value, service lives and annual depreciation expense of all debt-funded assets included in the wholesale portion of SFWD utility plant in service as of June 30, 1983 shall be as shown in Exhibit B-1. (No depreciation expense will continue for any asset once that asset has no remaining service life; however, such assets will continue to be included in the rate base at their salvage value, if any.) Assets added to the wholesale portion of SFWD utility plant after June 30, 1983 shall be assigned reasonable service lives and salvage values consistent with waterworks industry standards and practices. Debt-funded assets scheduled to be added during FY 1983/84 shall be assigned service lives as shown in Exhibit B-5.

Depreciation shall be calculated on a straight line basis.

The suburban purchasers' share of depreciation on each asset in the SFWD wholesale utility plant shall be equal to the total annual depreciation on each such asset times the suburban share of such asset (i.e., the percentage of each asset which has been allocated to the suburban purchasers for return on rate base purposes, as provided above). The total annual SFWD depreciation charge shall be equal to the sum of the suburban depreciation of each asset in the SFWD wholesale utility plant.

Section 4.08. *Suburban Hetch Hetchy Assessment.*

Description:

The Suburban Hetch Hetchy Assessment ("Assessment") is the charge assessed by the City to the suburban purchasers for the delivery of water by the Hetch Hetchy Water and Power Department ("HHWPD") from the Sierra watersheds to the SFWD's Alameda East Portal in Alameda County.

The Assessment consists of the suburban purchasers' share of

- the water-related portion of HHWPD operating expenses;
- the water-related portion of HHWPD maintenance expenses;
- the water-related portion of HHWPD property taxes;
- return on the water-related HHWPD rate base;
- depreciation on the water-related HHWPD utility plant.

Calculation:

Calculation of the Assessment entails two steps.

First, the water-related share of HHWPD operating and maintenance expenses and property taxes, the return on water-related rate base and depreciation on water-related utility plant must be determined.

Second, the suburban purchasers' share of these items must be determined.

(a) *Calculation of Water-Related Portion of HHWPD Expenses, Property Taxes, Return and Depreciation.*

(1) *Operating Expenses.*

Description: This category consists of expenses incurred in operating physical facilities within the HHWPD jurisdiction and related administrative and general expenses. Expenses associated exclusively with the production and distribution of hydroelectric power (e.g., purchased power, wheeling charges, rental of power lines and operation of SF Municipal Railway (MUNI) overhead lines) are categorized as power-specific and are not allocated to water. In addition, expenses associated with operating power facilities such as generating plants and transmission lines are also categorized as power-specific and are not allocated to water. Expenses associated with the operation of facilities which serve both the water and power functions (such as dams) are categorized as "joint" and are allocated to each function as described below. Expenses associated exclusively with the operation of facilities which serve only the water function (such as water transmission pipelines) are categorized as water-specific and are allocated entirely to water.

Allocation: Water-specific operating expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-1. These expenses shall be allocated entirely to water.

Power-specific operating expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-1. These expenses shall be allocated entirely to power.

Joint operating expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-1. These expenses shall be allocated 55% to power and 45% to water, except for City overhead and SFPUC charges, which shall be allocated as follows:

(A) *City Overhead.*

Description: This category consists of support services provided by the City's central service departments which have not been directly billed to HHWPD or other operating departments, as described in Section 4.04(a). The HHWPD's share of these costs is presently identified in the HHWPD cost ledgers as account No. 840920-0920.

Allocation: For purposes of this Agreement, the City overhead allocable to the HHWPD shall be "deemed" in the same manner and be subject to the same restrictions as City overhead is "deemed" to the SFWD and the SFPUC pursuant to Section 4.04(a). For FY 1984/85, the City overhead allocable to the HHWPD shall be deemed to equal $250,000. Thereafter, the HHWPD share of City overhead shall increase or decrease to reflect changes in the San Francisco-Oakland Metropolitan Area Consumer Price Index through FY 1988/89. After FY 1988/89, the HHWPD share of City overhead shall be determined through the negotiation/arbitration process set forth in Section 4.04(a).

City overhead costs allocated to the HHWPD in accordance with Section 4.04(a) and (b) and the preceding paragraph shall in turn be reallocated to water on the basis of a percentage derived from a fraction, the numerator of which is the sum of all HHWPD water-related operating and maintenance expenses as defined herein for the fiscal year in question, including 45% of joint operating and maintenance expenses but excluding City overhead and SFPUC charges, and the denominator of which is the total HHWPD operating and maintenance expenses, including all water-specific, joint and power-specific expenses, but excluding purchased power charges, wheeling charges,

rental of power lines, City overhead and SFPUC charges. The formula for allocation of City overhead costs is shown in Exhibit G-2.

(B) *Public Utilities Commission Charges.*

Description: This category consists of support services provided by the San Francisco Public Utilities Commission and its constituent bureaus to the HHWPD and the other operating departments under the jurisdiction of the SFPUC. For purposes of this Agreement, the expenses of such services shall be divided into two categories, "Class A" and "Class B." Class A services are those the costs of which are either assigned among departments based on a direct identification of use or on the basis of an allocation statistic other than the department's total expenditures, including all operating and capital expenditures. Examples of costs in this category presently include safety, training and claims processing expenses of the Bureau of Administration and the computer support from the Bureau of Management Information Systems. Class B services are those the costs of which are allocated on the basis of the departments' total expenditures, including all operating and capital expenditures. Examples of costs in this category presently include accounting and budget and analysis functions of the Bureau of Finance. The SFPUC charge, both Class A and Class B, is presently identified in the HHWPD cost ledgers as Account No. 840920-3600.

SFPUC charges shall be allocated to HHWPD in the same manner and subject to the same restrictions as such charges are allocated to SFWD, as described in Section 4.04(b).

Allocation: SFPUC charges allocated to HHWPD shall be reallocated between water and power as follows:

(i) Class A charges: Class A SFPUC charges allocated to HHWPD shall be reallocated to water on the basis of a percentage derived from a fraction the numerator of which is the sum of all water-related HHWPD operating and maintenance expenses, as defined herein, for the fiscal year in question, including 45% of joint operating and maintenance expenses, but excluding City overhead and SFPUC charges, and the denominator of which is total HHWPD operating and maintenance expenses but excluding purchased power, wheeling charges, rentals of power lines, maintenance of MUNI overhead lines expenses, City overhead and SFPUC charges.

The formula for allocation of Class A SFPUC costs is shown in Exhibit G-2.

(ii) Class B charges: Class B SFPUC charges allocated to HHWPD shall be reallocated to water on the basis of a percentage derived from a fraction the numerator of which is the sum of all HHWPD water-related operating and maintenance expenses, as defined herein, for the year in question, including 45% of joint operating and maintenance expenses (but excluding City overhead and SFPUC charges) plus water-related capital outlays, however funded, including 45% of capital outlays on joint facilities, and the denominator of which is total HHWPD operating and maintenance expenses, including all water-specific, joint and power-specific expenses (except City overhead and SFPUC charges), plus total HHWPD capital outlays, however funded.

Total HHWPD operating and maintenance expenses shall, for purposes of this subsection (ii), include purchased power, wheeling and rentals of power lines expenses of HHWPD, if each is included in the HHWPD's total expenditures for purposes of allocating SFPUC expenses to it. If one or more of such expenses are excluded from the definition of total budget for purposes of the initial allocation to the operating departments, it or they shall similarly be excluded in this formula for allocation of Class B SFPUC charges between water and power.

The formula for allocation of Class B SFPUC costs is shown on Exhibit G-2.

(2) *Maintenance Expenses.*

Description: This category consists of expenses incurred in maintaining physical facilities within the HHWPD jurisdiction and related administrative and general expenses. Expenses associated exclusively with maintaining power facilities such as generating plants, transmission lines and MUNI overhead lines are categorized as power-specific and are not allocated to water. Expenses associated with maintaining facilities which serve both the water and power functions (such as dams) are categorized as "joint" and are allocated to each function as described below. Expenses associated exclusively with the maintenance of facilities which serve only the water function (such as water transmission lines) are categorized as water-specific and are allocated entirely to water.

Allocation: Water-specific maintenance expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-3. These expenses shall be allocated entirely to water.

Power-specific maintenance expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-3. These expenses shall be allocated entirely to power.

Joint maintenance expenses presently consist of the line items in the HHWPD cost ledgers so designated on Exhibit G-3. These expenses shall be allocated 55% to power and 45% to water.

(3) *Property Taxes.*

Description: This category consists of ad valorem property taxes levied against HHWPD properties located in Tuolumne, Stanislaus, San Joaquin and Alameda Counties. These are presently identified in the HHWPD cost ledgers as Account No. 840928-1425.

Allocation: All property taxes paid by HHWPD shall be deemed a joint expense and shall be allocated to water on the basis of a "utility plant percentage" derived from a fraction, the numerator of which is the average-for-the-year net book value of all HHWPD water-related assets located outside the City's geographical limits, however funded (including 45% of all HHWPD joint assets located outside the City's geographical limits, however funded) and the denominator of which is the average-for-the-year net book value of all HHWPD assets located outside the City's geographical limits, however funded. An illustration of the formula for allocation of property taxes is shown on Exhibit G-4.

(4) *Calculation of Return on Water-Related Portion of HHWPD Rate Base.*

The return on the water-related portion of the HHWPD rate base is the product of (1) the water-related portion of the total HHWPD rate base times (2) the overall rate of return. Each component shall be calculated as set forth below.

(i) *Calculation of Water-Related Portion of HHWPD Rate Base.*

The water-related portion of HHWPD rate base used for calculating return shall be the sum of (1) the average of the water-related portion of HHWPD net utility plant in service at the beginning of the year and the water-related portion of HHWPD net utility plant in service at the end of the year (i.e., the beginning water-related portion of HHWPD net utility plant in service plus capital additions less depreciation, retirements and other dispositions removing an asset from utility plant in service) and (2) a water-related HHWPD working capital allowance equal to one-sixth (1/6) of the HHWPD water-related operating expenses and maintenance expenses, as defined above, which do not include property taxes.

The water-related portion of HHWPD net utility plant shall be the sum of the net book values, determined on the basis of depreciated original cost, of: (1) all bond-funded, water-specific HHWPD assets included in net utility plant in service as of June 30, 1984; (2) 45% of the net book value of all bond-funded, joint HHWPD assets included in net utility plant in service as of June 30, 1984; and (3) all water-specific and a portion of all joint HHWPD assets, however funded, added to net utility plant in service after June 30, 1984, except for assets, or portions thereof, funded from federal or state grants or direct user contributions. Thus, assets added to utility plant during fiscal year 1983/84 and funded from revenue shall not be included in the HHWPD water-related rate base for

purposes of this Agreement. (A list of the revenue-funded assets which the City expects to add to the HHWPD utility plant during fiscal year 1983/84 is shown in Exhibit H-3; these assets will not be included in the HHWPD water-related rate base for purposes of this Agreement regardless of whether they are actually placed into service during FY 1983/84 or thereafter.)

If the City finances the acquisition of new assets for the HHWPD by means other than from revenues or through bonded debt (e.g., by means of leases), the capitalization of those assets, the treatment of related expenses and related debt, and all other aspects of their accounting treatment, for purposes of this Agreement, shall be in accordance with Generally Accepted Accounting Principles, as amended from time to time.

The net book value of all debt-funded assets included in net utility plant in service as of June 30, 1983 and their categorization as power-specific, water-specific or joint is shown in Exhibits H-1 and H-2. The City will furnish the Suburban Representatives a list of all debt-funded assets, together with the asset number, category, net book value, service life and annual depreciation for each, added to the HHWPD water-related utility plant during FY 1983/84. This list will be delivered on or before December 31, 1984.

The categorization of new assets as water-specific, power-specific or joint and the portion of new joint assets to be allocated to water-related net utility plant in service after June 30, 1983 shall be as agreed upon by the parties and, in the event they are unable to agree, by arbitration as provided in Section 8.02. The arbitrator shall be directed to resolve the dispute by reference to accepted cost-allocation methodologies (or modifications thereof) and in a way which fairly allocates the cost of a new facility to or between the function(s) which it will serve. Debt-funded assets scheduled to be added during FY 1983/84 shall be categorized as shown in Exhibit H-4.

Interest on new debt-funded assets shall be capitalized in accordance with applicable Generally Accepted Accounting Principles, as amended from time to time.

(ii) *Calculation of Overall Rate of Return.*

The overall rate of return on the water-related portion of HHWPD rate base is equal to the sum of (1) the product of the cost of HHWPD water-related debt times the HHWPD water-related debt percentage and (2) the product of the return on HHWPD water-related equity times the HHWPD water-related equity percentage.

Each of these terms shall be defined and/or derived as follows:

(1) The cost of HHWPD water-related debt is the water-related debt interest expense for the year divided by the average outstanding balance of water-related debt. At any given date, water-related debt outstanding is that portion of total debt outstanding, the proceeds of which have been used to finance the construction or acquisition of water-related assets included in HHWPD net utility plant in service, as of that date. The average outstanding balance of HHWPD water-related debt is the beginning of the year balance plus the end of the year balance, divided by 2. The cost of HHWPD water-related debt for FY 1983/84 is estimated to be 3.8936%, as shown in Exhibit D-2.

(2) The HHWPD water-related debt percentage is the percentage obtained by dividing the average outstanding balance of HHWPD water-related debt by the sum of (a) the average-for-the-year net book value of water-related assets, as defined above, plus (b) the water-related HHWPD working capital allowance, as defined above.

The HHWPD water-related debt percentage for FY 1983/84 is estimated at 14.27%. In subsequent years, water-related HHWPD debt shall include all outstanding City debt the proceeds of which are used to construct or acquire water-specific HHWPD assets and a portion of all outstanding City debt the proceeds of which are used to construct or acquire joint HHWPD assets. The water-related portion of any debt issued in the future, some or all of which is used

to construct or acquire HHWPD assets, shall be equal to a fraction, the numerator of which shall be the original cost of water-related utility plant assets financed by the proceeds of such debt (determined as provided in Section 4.08(a)(4)(i)) and the denominator of which shall be the total proceeds of such debt.

The water-related share of currently outstanding debt shall be as shown in Exhibit D-2.

(3) The return on HHWPD water-related equity shall be equal to the return on SFWD wholesale equity defined in Section 4.06(c)(iii).

(4) The HHWPD water-related equity percentage is equal to 100% minus the HHWPD water-related debt percentage.

The methodology for calculating the overall rate of return on HHWPD water-related rate base is shown on Exhibit F-2.

(5) *Calculation of HHWPD Water-Related Depreciation.* Water-related depreciation is the annual depreciation expense on the original cost of assets in the water-related portion of HHWPD utility plant in service. The "original cost" of each asset used for calculating depreciation for purposes of this Agreement shall be equal to the original cost of each asset in the water-related portion of HHWPD utility plant in service minus any revenue-funded portions thereof (including capitalized interest funded from revenue) added to the rate base prior to June 30, 1984 and any portion of the asset financed from federal or state grants or direct user contributions.

The original cost, salvage value, service lives and annual depreciation expense of all debt-funded water-related assets included in HHWPD utility plant in service as of June 30, 1983 shall be as shown in Exhibit H-1. (No depreciation expense will continue for any asset once that asset has no remaining service life; however, such assets will continue to be included in the rate base at their salvage value, if any.) Water-related assets added to utility plant after June 30, 1983 shall be assigned reasonable service lives and salvage values consistent with waterworks industry standards and practices. Debt-funded assets scheduled to be added during FY 1983/84 shall be assigned service lives as shown in Exhibit H-4.

Depreciation shall be calculated on a straight line basis.

(b) *Calculation of Suburban Purchasers' Share of Suburban Hetch Hetchy Assessment.*

The suburban purchasers' share of the Assessment shall be calculated as follows:

(i) The suburban purchasers' share of HHWPD water-related operating expenses, maintenance expenses and property taxes shall be derived by multiplying the total of such expenses times the suburban current base rate, times a fraction, the numerator of which is the amount of water delivered to the SFWD by HHWPD during the fiscal year and the denominator of which is the amount of water delivered by the HHWPD to all users who receive water from it, during that year.

(ii) The suburban purchasers' share of return on HHWPD water-related rate base and water-related depreciation shall be derived by multiplying each times the suburban ultimate base rate (64.56%), times a fraction the numerator of which is the amount of water delivered to the SFWD by HHWPD during the fiscal year and the denominator of which is the amount of water delivered by the HHWPD to all users who receive water from it, during that year.

ARTICLE V

INTEGRATION OF SUBURBAN REVENUE REQUIREMENT WITH SFWD BUDGET DEVELOPMENT AND RATE ADJUSTMENTS

Section 5.01. *General Purpose.*

The purpose of the allocational formulas set forth in Article IV is to determine the suburban revenue requirement for each fiscal year. The suburban revenue requirement can only be estimated in advance, based upon projected costs and water usage. These projections will be used to establish rates applicable to the suburban purchasers, which rates will be designed to produce the estimated suburban revenue requirement.

After the close of each fiscal year, the procedures described in Article VI will be conducted to determine the actual suburban revenue requirement, based on actual costs incurred, allocated according to the formulas agreed upon, and utilizing actual water usage data. The amount properly allocable to the suburban purchasers pursuant to this Agreement shall be compared with the actual revenues received from the suburban purchasers during the fiscal year under review, as shown in the official accounting records of the SFWD. If the actual payment by the suburban purchasers is less than or more than the amount properly allocable to them under this Agreement (i.e., the actual suburban revenue requirement), the amount of the excess or deficit shall be entered in a "balancing account" (as described in Section 5.07) to be charged or credited to the suburban purchasers, as the case may be.

The amount of such charge or credit shall then be taken into account in determining the necessity for rate increases or decreases in the next ensuing fiscal year (e.g., FY 1986/87 for the amount posted to the balancing account for FY 1984/85) in the manner described in Section 5.07(b). Rates for the suburban purchasers will be increased or decreased as necessary to reflect the amount in the balancing account and the estimated suburban revenue requirement for that year, in accordance with the provisions of Section 5.07(b).

Section 5.02. *Budget Development.*

Two weeks before the submission of the annual SFWD and HHWPD budgets to the City's Public Utilities Commission, the General Manager of the SFWD and the General Manager of the HHWPD shall meet with the suburban purchasers to review and explain the proposed budgets of each Department for the ensuing fiscal year. The General Manager of the SFWD and the General Manager of the HHWPD may each designate an appropriate official of their respective departments to attend this meeting in his or her place, if, because of illness or other reasons beyond their control, he or she is unable to attend. Each suburban purchaser may nominate no more than one representative to attend this meeting and the City shall not be obligated to hold more than one such budget review meeting with the suburban purchasers in each fiscal year.

At least two weeks before this meeting, the City shall mail copies of the following documents to the Suburban Representatives appointed pursuant to Section 8.13:

1. Proposed SFWD operating and capital budgets for the ensuing fiscal year.
2. The SFWD's and HHWPD's most recent update of the current year's expenditures (the organization management performance report) and the balance sheet and income statement for the most recent fiscal year, if available.
3. Proposed HHWPD operating and capital budgets for the ensuing fiscal year.
4. Detailed calculation of the proposed Suburban Hetch Hetchy Assessment.
5. Projected bond sales, if any, for SFWD and HHWPD for the ensuing fiscal year.
6. Estimated City and Suburban consumption for the ensuing fiscal year.

Thereafter, the budget request of the General Manager of Utilities shall be sent to the Suburban Representatives at the same time it is sent to the SFPUC. Except for changes authorized by Section 5.03(b), any proposed changes in the structure of the rate schedule(s) applicable to the suburban purchasers for the ensuing fiscal year shall similarly be sent to the Suburban Representatives by five months prior to the start of the fiscal year or whenever they are available, whichever is sooner. All suburban purchasers shall be notified at least five days in advance of the date on which the SFPUC will hold hearings on the budget request.

The City will use its best efforts to provide the documents and hold the meetings in accordance with the foregoing schedule. However, the failure of the City to comply with the requirements set forth in this Section shall not invalidate any action taken by the City (including, but not limited to, any rate increase or decrease adopted by the City). In the event of such failure, the suburban purchasers may either invoke arbitration, as set forth in Section 8.02, or seek injunctive relief, to compel the City to remedy the failure as soon as is reasonably practical, and the City shall be free to oppose issuance of the requested judicial or arbitral relief on any applicable legal or equitable basis. The existence of this right to resort to arbitration shall not be deemed to preclude the right to seek injunctive relief.

The provisions of this Section requiring a meeting with the General Managers are not intended to preclude the suburban purchasers from appearing before the SFPUC or the City Board of Supervisors concerning the SFWD budget and/or suburban water rates.

Section 5.03. *Rate Adjustments.*

(a) *Budget-Coordinated Rate Adjustments.* Adjustments to the SFWD rate schedules that affect the suburban purchasers shall be coordinated with the budget development process in the manner set forth in this Section except to the extent that Section 5.03(b) authorizes emergency rate adjustments.

Should the City desire to increase the rates applicable to the suburban purchasers during the ensuing fiscal year in conjunction with the budget development process, the General Manager of Utilities shall prepare and distribute to the Suburban Representatives at the same time and in addition to the information required to be sent to the Suburban Representatives by Section 5.02, a tabulation based on the most recent budget which shows the following data:

(i) Projected revenue from the suburban purchasers for the ensuing fiscal year based on existing rates and estimated suburban consumption.

(ii) An estimate of how projected SFWD operating and maintenance expenses and property taxes for the ensuing fiscal year will be allocated between direct City, joint, and direct suburban categories pursuant to the methodology set forth in this Agreement and an estimate of how the joint operating and maintenance expenses and property taxes will be allocated between the suburban purchasers and the City pursuant to the methodology set forth in this Agreement.

(iii) Calculation of projected SFWD administrative and general expenses (including an estimate of how projected City overhead and the SFPUC charges will be allocated to the SFWD pursuant to the methodology set forth in this Agreement) and an estimate of how these administrative and general expenses will be allocated between the City and the suburban purchasers pursuant to the methodology set forth in this Agreement.

(iv) The projected Hetch Hetchy Assessment (including an estimate of how projected City overhead and the SFPUC charges will be allocated to HHWPD pursuant to the methodology set forth in this Agreement), and an estimate of how HHWPD expenses (including City overhead and SFPUC charges) will be allocated between water and power pursuant to the methodology set forth in this Agreement.

(v) Description of the assets to be added to the SFWD wholesale rate base and the HHWPD water-related rate base in the next fiscal year, including the proposed assignment of such assets into the categories described in Article IV and the resulting allocation of such assets between the City and the suburban purchasers; computation of the projected effective interest rate on

outstanding SFWD wholesale debt and outstanding HHWPD water-related debt; and the projected rate of return on equity for the SFWD wholesale rate base and the HHWPD water-related rate base.

In addition to the foregoing, the City shall distribute to the Suburban Representatives (i) copies of any proposed changes in the rate schedules, together with supporting documentation, at the time such materials are forwarded from the General Manager of the SFWD to the General Manager of Utilities; and (ii) copies of any proposed resolution submitted to the SFPUC calling a hearing on the proposed changes to the rate schedules, at the time such proposed resolution is submitted to or adopted by the SFPUC, whichever is earlier. At the time the material in (i), *supra*, is furnished to the Suburban Representatives, the Suburban Representatives shall also be sent the calculations required to be performed by Section 5.07(b) of the Estimated Suburban Revenue Requirement for the fiscal year for which rates are being set, the Revenue Discrepancy to be used for that fiscal year, and the Estimated Suburban Payment for that year.

The City will use its best efforts to provide the suburban purchasers with the information described above. However, the failure of the City to comply with the requirements set forth in this Section shall not invalidate any action taken by the City (including, but not limited to, any rate increase or decrease adopted by the City). In the event of such failure, the suburban purchasers may either invoke arbitration, as set forth in Section 8.02, or seek injunctive relief, to compel the City to remedy the failure as soon as is reasonably practical, and the City shall be free to oppose the issuance of the requested judicial or arbitral relief on any applicable legal or equitable basis. The existence of this right to resort to arbitration shall not be deemed to preclude the right to seek injunctive relief.

Because delays in the budget process or other events may cause the City to defer the effective date of rate adjustments applicable to the suburban purchasers until after the beginning of the City's fiscal year, nothing contained in this Agreement shall require the City to make any changes in the water rates charged to the suburban purchasers effective at the start of the City's fiscal year or at any other specific date. Nothing in the preceding sentence shall excuse non-compliance with the provisions of Section 5.02 and this Section.

(b) *Emergency Rate Increases.*

(1) The City may increase the water rates applicable to the suburban purchasers without complying with Section 5.03(a) if a drought, earthquake, other act of God, malfunctioning of the City's water delivery system or other emergency requires an increase in rates, prior to the date by which a rate increase adopted in conjunction with the next budget-coordinated rate review would become effective, to meet the SFWD's wholesale or the HHWPD's water-related estimated operating and capital expenses (i.e., debt service and capital outlays) in light of the emergency. Rates may be increased under this subsection to cover capital expenses only if the SFWD does not have sufficient unappropriated funds available for use and is unable to obtain sufficient funds, in the time necessary, through the issuance of bonds or from State or federal grants. Rates may be increased under this subsection to cover operating expenses (including Operating and Maintenance expenses and Administrative and General expenses) without regard to the existence of alternative means of financing such expenses. Any such emergency rate increase shall be accompanied by a rate increase for direct City water users of at least an equal percentage. Any such emergency rate increase need not be spread uniformly within the two classes (i.e., the class of direct City water users and the class of suburban purchasers) as long as the overall percentage increase for the suburban purchasers is no greater than the overall percentage increase for the direct City water users.

(2) The City may increase the water rates applicable to the suburban purchasers without complying with Section 5.03(a) to implement a water allocation plan imposed during times of water shortage pursuant to Section 7.03, as long as such changed rates impose no greater burdens on the suburban purchasers than on direct City water users for failure to abide by the allocation plan.

(3) The City will give the Suburban Representatives no less than ten days notice of the hearing before the SFPUC on a proposed emergency rate increase under Section 5.03(b)(1) or 5.03(b)(2); however, the failure of the City to provide such notice shall not invalidate any action taken by the City (including, but not limited to, any rate increase adopted by the City) unless the City has failed to substantially comply with this notice requirement. Any revenue derived from rates increased pursuant to Section 5.03(b)(1) or 5.03(b)(2) shall be subject to the balancing account described in Section 5.07. No rate increase authorized by Section 5.03(b)(1) or 5.03(b)(2) shall remain in effect for longer than eighteen months.

Section 5.04. *Rate Structure.*

Prior to August 1, 1983, the City determined water bills for individual suburban purchasers by reference to Schedule W-25 (Resale Use with Long Term Contract) contained in the Rate Schedules for Water Service as established by Resolution 79-0474 of the SFPUC on November 27, 1979. The City has amended this rate schedule, effective August 1, 1983 and expects to amend the rate schedule(s) applicable to the suburban purchasers additionally as needed during the Term of this Agreement to generate the estimated suburban revenue requirement for each fiscal year. This Agreement is not intended and shall not be construed to limit the City's right to adjust the structure of the rate schedule applicable to the suburban purchasers (i.e., the relationship among the several charges set out therein) nor shall anything in this Agreement be construed to limit the City's freedom to add, delete, or change the various charges which make up the rate schedule, provided that neither such charges nor the structure of the rate schedule(s) applicable to the suburban purchasers shall be arbitrary, unreasonable, or unjustly discriminatory as among said purchasers. (Nothing in the preceding sentence shall be construed or interpreted in derogation of the waiver in Section 5.05 of any claim by the suburban purchasers that the suburban revenue requirement, as determined by the provisions of and the methodology provided by this Agreement, is illegal, unreasonable, arbitrary or discriminatory in any manner.) The City will give careful consideration to proposals for changes in the rate schedule made jointly by the suburban purchasers but, subject to the limitations set out above, shall retain the sole and exclusive right to determine the structure of the rate schedule. The City will not change the structure of Schedule W-25 for three years (i.e., until the rates applicable to FY 1987/88) in order to allow time for the suburban purchasers to complete and submit a study of the rate schedule's structure now underway and for the SFPUC to consider it. Notwithstanding the preceding sentence, the City shall be free to make changes in the structure of the rate schedule within the three-year period to implement a water allocation plan imposed during times of water shortage pursuant to Section 7.03, provided that any such changed rate schedule shall impose no greater burdens on the suburban purchasers than on direct City users for failure to abide by the allocation plan. The City will endeavor insofar as it is reasonably practical to set forth the rates applicable to the suburban purchasers on a single rate schedule.

Section 5.05. *Waiver and Reservation re Methodology for Determining Suburban Revenue Requirement.*

(a) The suburban purchasers have heretofore asserted a right to water at cost by reason, among others, of rights claimed to be conferred by the Raker Act, and City has heretofore denied such assertions and claims. The purpose of this Agreement is to settle and compromise the different positions of the parties hereto as to said assertions and claims for the Term of this Agreement and nothing contained herein shall constitute an admission by any party hereto affecting, modifying, abrogating, limiting, or conceding its position as regards such assertions and claims, or as a waiver of its position, either in whole or in part. In particular, and without limitation, the suburban purchasers do not waive, and specifically reserve, their claim that the methodology employed under this Agreement for determination of the suburban revenue requirement (the "utility enterprise method") is not proper or valid under state and federal law (including, but not limited to, the Raker Act) and the

City does not waive, and specifically reserves, its claims that said methodology is proper and valid and does not violate state or federal law (including, but not limited to, the Raker Act), and that the rates generated by said methodology will produce less revenue to the City than would be justified by the full cost of the water delivered or is otherwise proper under state or federal law (including, but not limited to, the Raker Act.)

(b) Notwithstanding subsection (a), *supra*, in order to effect the settlement and compromise of the disputes of the parties during the Term of this Agreement, each suburban purchaser hereby covenants and agrees on its own behalf, and on behalf of all persons and entities to which it sells water, that it will not contend, during the Term of this Agreement, before any court or administrative tribunal or official, that the suburban revenue requirement, as determined by the provisions of and the methodology provided by this Agreement violates any provision of federal law (including, but not limited to, the Raker Act), state laws or the Charter of the City and County of San Francisco, or is unfair, illegal, unreasonable, arbitrary or discriminatory in any manner, except that the suburban purchasers expressly reserve, as provided in Section 8.01, the right to so contend as to any attempt by the City to include a charge for reduced net power revenues in the price of additional water over the amount specified in the Supply Assurance set forth in Section 7.01.

(c) Nothing contained in this Section shall prevent any suburban purchaser from pursuing any remedy provided by this Agreement for breach or violation of this Agreement or from seeking to enforce performance of the Agreement's terms and conditions.

Section 5.06. *Exclusions from Rate-Making Procedures.*

(A) The suburban purchasers shall not be charged with any of the following:

(1) any expense associated with the City's furnishing free water to its municipal departments (sometimes heretofore identified in the SFWD accounts as "Municipal Tax-Comparison");

(2) any expense associated with the City's accruals or allowances for uncollectible water accounts;

(3) any expense incurred by the City in hiring outside counsel to assist in arbitration and/or litigation concerning the respective rights and obligations of the City and the suburban purchasers under this Agreement;

(4) attorneys' fees incurred by the suburban purchasers which a court of competent jurisdiction orders the City to pay as part of a final, binding judgment against the City;

(5)(a) any expenses associated with creating or maintaining any reserves (other than the working capital component included in the SFWD and HHWPD rate bases, depreciation, and reserves for accounts payable expenses accrued and expected to be paid within one year, all as provided in Article IV);

(b) any expenses accrued in respect to pending or threatened litigation, damage or personal injury claims and other loss contingencies, accruals of which are required by the Financial Accounting Standard Board Statement No. 5 (March 1975) as amended; such expenses will, to the extent provided in Article IV, be charged to the suburban purchasers when they are actually paid;

(6) any expenses of installing, relocating, enlarging, removing, or modifying meters and service connections that are directly chargeable to and payable by the individual suburban purchaser for which the service is rendered pursuant to Section 8.15; or

(7) any expenses associated with the provision by the SFWD or the HHWPD to a suburban purchaser of any good or service other than the sale of water.

(B) The suburban purchasers shall not receive any credit for either of the following:

(1) any SFWD or HHWPD non-operating revenue or interest earned on SFWD or HHWPD funds;

(2) any HHWPD income derived from water sales to persons or entities other than the SFWD.

Section 5.07. *Balancing Account.*

(a) *Operation.* After the close of each fiscal year, the City will compute the amount properly allocable to the suburban purchasers for that fiscal year pursuant to this Agreement based upon the actual costs incurred by the SFWD and HHWPD during the year in the categories described in Article IV and the actual suburban water usage rates, based upon the records of water deliveries maintained by the SFWD and HHWPD. This amount ("the final suburban revenue requirement" described in Section 6.02) will be compared to the actual revenues received from the suburban purchasers during the fiscal year under review, as shown in the official accounting records of the SFWD.

If the actual revenues received from the suburban purchasers for sales of water are more than the final suburban revenue requirement, the amount of the excess shall be posted to a "balancing account" to the credit of the suburban purchasers. If the actual revenues received from the suburban purchasers for sales of water are less than the final suburban revenue requirement, the amount of the deficit shall be posted to the balancing account as a charge against the suburban purchasers. There shall also be posted to the balancing account interest for the fiscal year under review equal to the product of the opening cumulative balance in the balancing account at the beginning of such year times the interest rate received by the City during such year on its invested pooled funds (as shown in the City Treasurer's Annual Report for that year). Interest, when posted, shall carry the same mathematical sign, whether positive or negative, as was carried by the opening cumulative balance for that year. The amount posted to the balancing account in each year shall be added to or subtracted from, as the case may be, the balance in the account from prior years to obtain the cumulative balance in the balancing account.

The parties recognize that a proposed amendment to the City Charter will be submitted to the voters of the City in June 1984 which would require that the Treasurer maintain all gross revenues of the SFWD in a separate fund whenever certain SFWD revenue bonds are outstanding. If this or a similar provision becomes effective and the City Treasurer is required to establish a "water department revenue fund" separate and apart from the funds of other City departments, the applicable interest rate for purposes of computing interest under this Section shall be the interest rate received by the SFWD on its invested funds and shall be calculated in the same manner as the Controller calculates the interest rate received by the City on its invested pooled funds.

There shall be no interest posted to the balancing account until the amount for the fiscal year ending June 30, 1988 has been posted to the balancing account. The first opening balance to which interest shall be added shall be the opening balance for fiscal year 1988/89.

(b) *Methodology for Utilizing Balancing Account in Budget Coordinated Rate Adjustment Process.* The purpose of this subsection is to establish a procedure which attempts to clear cumulative balances in the balancing account by taking previously posted overcharges or undercharges by the City into account for prospective rate making purposes, in accordance with the methodology described in this subsection. However, this methodology shall have no effect whatsoever upon the amount actually posted to the balancing account for any particular fiscal year or upon the cumulative balance in the balancing account. These matters shall in all cases be determined in accordance with Section 5.07(a), based upon the actual revenues received from the suburban purchasers in that year and the Final Suburban Revenue Requirement for that year, as audited in accordance with Article VI.

For prospective rate making purposes, whether rates applicable to the suburban purchasers are to be increased or reduced for a particular fiscal year shall be determined by a comparison between the Estimated Suburban Payment and the Adjusted Estimated Suburban Revenue Requirement for that year, in accordance with the following methodology:

In conjunction with the budget development process described in Sections 5.02 and 5.03, the City shall estimate, without regard to the amount in the balancing account, (1) the suburban revenue requirement for the fiscal year for which the budget is being developed (the "Estimated Suburban Revenue Requirement"), and (2) the total suburban payments which would be made during that fiscal year at existing rates and projected levels of water consumption, (the "Estimated Suburban Payment").

The Estimated Suburban Revenue Requirement shall then be adjusted by subtracting therefrom the Revenue Discrepancy (as defined in the next paragraph) to produce the "Adjusted Estimated Suburban Revenue Requirement." (For example, in setting rates for the fiscal year 1990/91, the City shall, in the fiscal year 1989/90, estimate the Estimated Suburban Revenue Requirement for 1990/91, and then shall subtract therefrom the Revenue Discrepancy to produce the 1990/91 Adjusted Estimated Suburban Revenue Requirement.)

The Revenue Discrepancy to be used for the fiscal year for which rates are being set (e.g., 1990/91) shall be determined as follows:

(1) In the fiscal year during which the rates are being set (e.g., 1989/90), the ending balance in the balancing account for the prior completed fiscal year (e.g., 1988/89) shall be determined. This procedure is described in Steps A and B of Exhibit O.

(2) To the ending balance in the balancing account for the prior completed fiscal year (e.g., 1988/89), there shall be added (a) estimated interest for the current fiscal year (i.e., the fiscal year in which the budget is being developed (e.g., 1989/90)), as shown in Step C-1 of Exhibit O, and (b) the Estimated Revenue Differential for the current fiscal year. The Estimated Revenue Differential shall be determined by subtracting from the Current Expected Suburban Payment (as defined below) for the current fiscal year (e.g., 1989/90), the Estimated Suburban Revenue Requirement (as defined hereinabove) for the current fiscal year (e.g., 1989/90). (The calculation of the Estimated Revenue Differential is described in Step C-2 of Exhibit O.) The sum resulting from the operations described in this sub-paragraph shall be called the Required Revenue Adjustment. (See Step C-3 of Exhibit O.)

(3) To the Required Revenue Adjustment there shall be added estimated interest for the fiscal year for which the budget is being developed (e.g., 1990/91). This procedure is described in Step C-4 of Exhibit O.

(4) The sum resulting from the additions described in sub-paragraphs (1) through (3) above is the Revenue Discrepancy to be used for the fiscal year for which rates are being set (e.g., 1990/91).

If the Adjusted Estimated Suburban Revenue Requirement for the fiscal year for which the rates are being set (e.g., 1990/91) exceeds the Estimated Suburban Payment for such fiscal year, then rates applicable to the suburban purchasers may be increased to generate the Adjusted Estimated Suburban Revenue Requirement ± $50,000, at projected levels of water consumption.

If the Estimated Suburban Payment for such fiscal year (e.g., 1990/91) exceeds the Adjusted Estimated Suburban Revenue Requirement for such year by more than two percent (2%), then rates applicable to the suburban purchasers shall be reduced to generate the Adjusted Estimated Suburban Revenue Requirement ± $50,000, provided that nothing contained in this Agreement shall either prohibit or compel a rate reduction if such excess is two percent (2%) or less.

The Current Expected Suburban Payment for any given fiscal year shall mean the amount of revenue expected to be received by the City in that fiscal year based on the rates which it adopted for that fiscal year and the levels of water consumption projected for that fiscal year when that fiscal year's rates were set.

In performing the algebraic operations required by the foregoing methodology, the proper signs, whether negative or positive, of the numbers to be added or subtracted shall be taken into account.

In ascertaining the Revenue Discrepancy pursuant to this subsection for any given fiscal year, final audited figures shall be used as that fiscal year's opening balance in the balancing account, the Actual Suburban Revenues Received in that fiscal year, the Final Suburban Revenue Requirement for that fiscal year, and that fiscal year's ending balance in the balancing account. If final audited figures are not available, unaudited figures shall be used, but only for the purposes of carrying out the methodology described in this subsection.

In applying the methodology described above, the interest rate used to calculate the estimated interest for the current fiscal year and the next fiscal year shall be equal to the interest rate which was applied to the opening balance in the balancing account for the immediately preceding completed fiscal year pursuant to Section 5.07(a). (For example, when setting rates for the fiscal year 1990/91, the interest rate used for calculating the estimated interest for fiscal year 1989/90 and fiscal year 1990/91 shall be equal to the interest rate specified in Section 5.07(a) for fiscal year 1988/89.)

In implementing the methodology described in this subsection, the following qualifications shall apply:

This subsection shall not apply to rate-making for the fiscal year 1985/86. This subsection shall apply to rate-making for the fiscal year 1986/87, but: (1) the opening balance for fiscal year 1984/85 shall be equal to zero; (2) the Estimated Revenue Differential for the fiscal year 1985/86 shall be deemed equal to zero; and (3) no interest charges, either actual or estimated, shall be used in applying the foregoing methodology to rate-making for that fiscal year. This subsection shall apply to rate-making for the fiscal year 1987/88, but no interest charges, either actual or estimated, shall be used in applying the foregoing methodology to rate-making for that fiscal year. This subsection shall apply to rate-making for the fiscal year 1988/89, but no interest charges shall be added pursuant to Steps B-2 (e.g., for fiscal year 1986/87) and C-1 (e.g., for fiscal year 1987/88) in Exhibit O in applying the methodology to rate-making for that year; the estimated interest rate to be applied for the fiscal year 1988/89 under Step C-4 of Exhibit O shall be the interest rate specified in subsection 5.07(a) which would have been applied to the cumulative balance in the balancing account for the fiscal year 1986/87 but for the moratorium on interest specified in subsection 5.07(a). This subsection 5.07(b) shall apply to rate-making for the fiscal year 1989/90, but: (1) no interest charges shall be added pursuant to Step B-2 in Exhibit O (i.e., interest for the fiscal year 1987/88); and (2) the estimated interest rate to be applied for the fiscal year 1988/89 (under Step C-1 of Exhibit O) and for the fiscal year 1989/90 (under Step C-4 of Exhibit O) shall be the interest rate specified in subsection 5.07(a) which would have been applied to the cumulative balance in the balancing account for the fiscal year 1987/88 but for the moratorium on interest specified in subsection 5.07(a).

In setting rates for each fiscal year thereafter during the Term of this Agreement, commencing with setting rates for the fiscal year 1990/91, the methodology described in this subsection shall apply without qualification.

(c) *Exclusions from Revenue.* For purposes of this Section, "actual revenues received from the suburban purchasers for sales of water" shall not include: (1) amounts, if any, paid by any suburban purchaser, pursuant to Section 8.14, for water delivered through the SFWD's in-City water distribution system, in excess of the average charge per ccf. of water it and the other suburban purchasers pay for water not delivered through the SFWD's in-City water distribution system; (2) any amount directly paid by a suburban purchaser for the installation, relocation, or removal of meters and service pursuant to Section 8.15, the City's W-41 rate schedule, and Section E(8) and (9) of the SFWD's Rules and Regulations Governing Water Service to Consumers, as they may be amended from time to time; or (3) any other amounts received by the SFWD from a suburban purchaser for goods or services other than the sale of water.

(d) *Arbitration.* The City's implementation of Section 5.07(a) and (b) is subject to the arbitration remedy provided in Section 8.02, in accordance with the limitations on that remedy provided for herein. In the event that the methods that the City has used to estimate suburban revenue requirements and/or suburban payments have caused a persistent cumulative credit to the suburban purchasers in the balancing account resulting in a cumulative balance of seven and one-half percent of the annual suburban revenue requirement for any individual fiscal year, the suburban purchasers may invoke the arbitration remedy set forth in Section 8.02 and the arbitrator shall have discretion to enter either or both of the following orders:

(1) If the arbitrator finds that the existence of such persistent, cumulative credit demonstrates that the procedures set forth above in Section 5.07(b) are not functioning to clear the balancing account, the arbitrator may enter an order that the City refund to the suburban purchasers the cumulative credit in the balancing account. This refund shall take the form of a credit divided into twelve equal monthly installments to be offset against the monthly water bills sent to the suburban purchasers during the fiscal year in which rates adopted in conjunction with the next budget-coordinated rate review following the arbitration award would become effective, provided that in no event will the refund be commenced later than 18 months from the arbitration award. The credit shall be allocated among the suburban purchasers in accordance with their pro rata share of all water purchased by the suburban purchasers from the City during the fiscal year immediately prior to the year in which the demand for arbitration was served.

(2) If the arbitrator finds that such an order is necessary to prevent a repetition of the persistent cumulative credit, the arbitrator may enter an order that the City cease using the method of estimating suburban revenue requirements and/or suburban payments that have caused the persistent cumulative credit to the suburban purchasers in the balancing account.

The arbitration remedy shall be the exclusive remedy for any claimed violation by the City of Section 5.07(a) and (b).

(e) *Disposition of Ending Balance.* After the expiration of the Term, the audit procedures described in Article VI will be performed for the final year of the Term and the cumulative ending balance in the balancing account (including the results of that year's operations) will be determined.

The ending balance, if a credit in favor of the suburban purchasers, will be refunded to the suburban purchasers and, if a charge against them, shall be collected from them. The refund or collection shall take the form of a credit or surcharge divided into twelve equal monthly installments to be offset against or added to the monthly water bills sent to the suburban purchasers during the fiscal year immediately following the determination of the ending balance (i.e., FY 2010/11). The credit or surcharge shall be allocated among the suburban purchasers receiving or subject to it (i.e., those purchasing water from the City during FY 2010/11) in accordance with their pro rata share of all water purchased by all suburban purchasers likewise receiving or subject to the credit or surcharge from the City during the last fiscal year of the Term (i.e., FY 2008/09). No suburban purchaser which is not purchasing water from the City during the year in which the credit or surcharge shall be subtracted from or added to the water bills (i.e., FY 2010/11) shall be entitled or subject to any portion of the credit or surcharge.

If this Agreement is extended beyond its present Term, or if the City and some or all of the suburban purchasers enter into a new contract, the parties to the extended Agreement or new contract may postpone their pro rata portion of the refund or surcharge described in this subsection until the end of the term of the extended Agreement or new contract.

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ARTICLE VI

ACCOUNTING PROCEDURES; COMPLIANCE AUDIT

Section 6.01. *City Accounting Practices.*

(a) *General Rule.* The City will maintain the accounting records of the SFPUC, the SFWD and the HHWPD in a format and level of detail sufficient to allow it to determine the annual suburban revenue requirement and to allow its determination of the suburban revenue requirement to be audited as provided in this Article.

(b) *SFWD.* The City will continue to maintain the accounting records of the SFWD in accordance with the Uniform System of Accounts for Class A Water Utilities as adopted and prescribed by the CPUC from time to time, insofar as it is applicable to publicly owned and operated utilities. In addition, the SFWD will maintain an account structure which segregates SFWD operating and maintenance expenses (and any administrative and general expenses as to which the location in which they are incurred is relevant) and utility plant by geographic location into in-City and wholesale categories.

(c) *HHWPD.* The City will continue to maintain the accounting records of the HHWPD in accordance with the Uniform System of Accounts for Class A Electric Utilities as adopted and prescribed by the CPUC from time to time, insofar as it is applicable to publicly owned and operated utilities. In addition, the HHWPD will maintain an account structure which segregates HHWPD expenses and utility plant into water-specific, power-specific and joint categories.

(d) *Utility Plant Ledgers.* Both the SFWD and the HHWPD will maintain a subsidiary utility plant ledger that contains unique identification numbers for all assets added to the rate base after June 30, 1983 and identifies the original cost, accumulated depreciation, and annual depreciation expense for each asset so capitalized.

(e) *Supporting Documentation.* The SFWD, the HHWPD and the SFPUC, as appropriate, will maintain documentation identifying and supporting

(1) the division of the SFPUC charge into "Class A" and "Class B" categories, as defined in Section 4.08(a)(1)(B);

(2) the portion of total interest expense related to each series of each bond issue;

(3) the portion of total bonded debt outstanding related to each series of each bond issue;

(4) the use of the proceeds of each bond issue in sufficient detail to permit the calculation of the SFWD and HHWPD debt/equity ratios, and the average outstanding balance and cost of SFWD wholesale debt and HHWPD water-related debt.

(f) *Accounting Principles.* The City shall record transactions of the SFPUC, SFWD and HHWPD in conformity with applicable generally accepted accounting principles, as amended from time to time, except if those principles are inconsistent with an explicit provision of this Agreement.

(g) *Changes in Accounts or Accounting Practices.* Subject to the foregoing provisions of this Section, the City, the SFPUC, the SFWD or the HHWPD may change their accounting systems, charts of accounts or account to which individual expenses are posted, provided that the allocation of any expense to the suburban purchasers pursuant to the methodology set forth in this Agreement shall not be changed in whole or in part merely because of a change in: (1) the account to which such expense is posted; (2) the accounting system or chart of accounts used by the City, the SFPUC, the SFWD or the HHWPD; or (3) the organizational structure of the SFPUC, SFWD or HHWPD. The SFPUC, SFWD, and HHWPD will make available to the Auditor appointed pursuant to Section 6.03 a copy of their charts of accounts for the beginning of the fiscal year in question and a copy of their charts of accounts for the end of the fiscal year so that the Auditor can identify all changes in the account structure. At the time the interim suburban revenue requirement is delivered to the Auditor, the City also will notify the Auditor in writing of any changes made during the fiscal year

in the City's policies for assigning assets and expenses to particular SFPUC, SFWD or HHWPD accounts, including changes in the allocational bases for assigning SFPUC costs to the SFWD and HHWPD. A copy of this notice will be sent to the Suburban Representatives.

(h) *Unavailability of Financial Data.* The parties recognize that financial data required for the calculation of the final suburban revenue requirement occasionally may be unavailable. In that event, the City shall substitute an estimate for the data which are unavailable.

The estimate shall: (1) be reasonable; (2) result in a fair allocation of the costs affected by the estimate; and (3) be derived through the use of a suitable estimating technique. Estimating techniques employed shall be consistently applied to comparable instances of unavailable data.

In any case in which estimated, rather than actual, data are used to calculate the final suburban revenue requirement, the City shall notify the Suburban Representatives thereof at the time the final suburban revenue requirement is furnished to the Auditor. The notice shall contain: (1) a description of the unavailable data and the estimate used in place thereof; (2) an explanation of the cause of the data's unavailability; (3) the assumptions underlying the City's estimate; and (4) a statement of whether the event which caused the unavailability is capable of being avoided in the future and, if so, how.

In addition, if, while preparing the interim suburban revenue requirement, the City discovers that data are likely to be unavailable and that an estimate will likely be required to prepare the final suburban revenue requirement, it shall notify the Suburban Representatives and the Auditor as soon as possible thereafter.

The City shall, upon request, meet with the Suburban Representatives to discuss the unavailability of data and the City's estimate therefor. The parties may agree to engage an independent accountant or consultant (other than the Auditor or the Suburban Auditor) to recommend a mutually acceptable estimate for the unavailable data.

If actual data for which an estimate is used become available within eighteen months after the receipt (as defined in Section 8.02) of the Auditor's Report for the fiscal year in which the estimated data were used in calculating the final suburban revenue requirement, then the difference between the suburban revenue requirement calculated using the estimated data and that calculated using the actual data shall be determined. If that difference is greater than one-half of 1 percent of the final suburban revenue requirement for the fiscal year in which estimated data were used, then the difference shall be taken into account as an adjustment to the suburban revenue requirement for the year in which the data become available.

In order to minimize the likelihood that necessary financial data will be unavailable, the City will maintain two sets of data which are stored in either microfiche form or in some form of electronic storage (e.g., on magnetic tape), one set of which will be kept in the vault at 425 Mason Street, or at some other secure location. Data for a given fiscal year shall be maintained for at least three years from the fiscal year's close.

This Section is not applicable to Exhibit J, Section D of which defines the procedures governing the unavailability of water use data necessary to perform the calculations set forth therein.

Section 6.02. *Calculation of Suburban Revenue Requirement.*

Within three months after the close of each fiscal year (commencing with fiscal year 1984/85) the City will prepare a document, substantially in the form of Exhibit I, showing the calculation of an interim suburban revenue requirement for the preceding fiscal year based upon recorded expenses and recorded water usage.

The interim suburban revenue requirement may be revised by the City during the course of the compliance audit described in Section 6.04 and shall be revised to reflect any changes in recorded expenses required as a result of the audit of the SFWD and HHWPD conducted pursuant to the

City Charter and any corrections in the recorded water usage data to reflect actual usage. At the close of the audit, the City shall prepare a document, substantially in the form of Exhibit I, showing the calculation of a final suburban revenue requirement, which shall be submitted to the Auditor as the basis for its report in accordance with Section 6.05.

The City will furnish these calculations of the interim and final suburban revenue requirements to the Suburban Representatives, and shall make available to the Suburban Representatives, upon their request, supporting documentation which contains the data, identification of the sources of the data, and calculations made by the City in deriving the interim and final suburban revenue requirements. Upon request, the City will provide the Suburban Representatives with an explanation of the calculation of the interim suburban revenue requirement. The Suburban Representatives shall be given access to and shall be permitted to copy, at their own expense, all data and worksheets relevant to the calculation of the interim and final suburban revenue requirements.

Section 6.03. *Appointment of Independent Auditor.*

(a) *Purpose.* The purpose of this section is to provide for an annual audit by an independent certified public accountant of the procedures followed and the underlying data used by the City in calculating the interim and final suburban revenue requirements for the preceding fiscal year, to determine whether the interim and final suburban revenue requirements have been calculated in accordance with the terms of this Agreement and whether amounts paid by the suburban purchasers in excess of or less than the final suburban revenue requirement have been posted to the balancing account, together with interest as provided in Section 5.07(a).

(b) *Method of Appointment.* The City's Controller shall select an independent certified public accountant ("the Auditor") to conduct the compliance audit described below. Subject to approval by the Controller and the General Manager of the SFWD, the Auditor shall have the authority to hire such consultants as it deems necessary or appropriate to assist in the audit. The Auditor may be the same independent certified public accountant as is hired by the Controller to audit the books and records of the SFWD and/or the HHWPD.

The costs of the compliance audit shall be segregated from the cost of other auditing work, if any, performed by the Auditor for the City and allocated one-half to the City and one-half to the suburban purchasers. The terms of this Article shall be incorporated into the contract between the City and the Auditor, and the suburban purchasers shall be deemed to be third-party beneficiaries of said contract. The City shall use its best efforts to see to it that the Auditor complies with the provisions of Sections 6.04 and 6.05, but shall not be liable to the suburban purchasers for any failure by the Auditor to comply with the said sections or to conduct the audit in compliance with generally accepted accounting standards.

Section 6.04. *Conduct of Compliance Audit.*

(a) *Standards.* The Auditor shall perform the compliance audit in accordance with Generally Accepted Auditing Standards. In particular, its review shall be governed by the standards contained in Section AU 621.09 through AU 621.13 (Reports on Specified Elements, Accounts or Items of a Financial Statement) of the AICPA, *Professional Standards,* as amended from time to time.

(b) *Preliminary Meeting; Periodic Status Reports; Access to Data.* Prior to commencing the audit, the Auditor shall meet with the City and the Suburban Representatives to discuss the scope of work, the procedures to be employed and the schedule to be followed. No change in the level of precision, confidence level or audit procedures defined in Section 6.04(c), however, may be made without the consent of both the City and the Suburban Representatives. During the course of the audit, the Auditor shall keep the City and Suburban Representatives informed of any unforeseen problems or circumstances which could cause a delay in the audit or a significant expansion of the audit's scope. The Auditor shall be given full access to all records of the SFWD, HHWPD and other City departments that the Auditor deems necessary for the audit.

(c) *Level of Precision and Audit Procedures.* The Auditor shall perform the audit based on a precision level of ±1 percent of the City's computation of the suburban revenue requirement for the fiscal year under audit, using a confidence level of 99 percent, for the compliance audits covering fiscal years 1984/85 through 1986/87 and a precision level of ± one-half of 1 percent (with the same confidence level) thereafter. The Auditor shall review the City's calculation of the interim and final suburban revenue requirements and the underlying data in order to carry out the purpose of the audit described in Section 6.03(a) and to issue the report prescribed by Section 6.05. At a minimum the Auditor shall perform the following procedures:

(1) *SFWD Operating and Maintenance Expenses.* The Auditor shall review the SFWD cost ledgers to determine whether the recorded operating and maintenance expenses fairly reflect the costs incurred, reasonably reflect the geographic location at which the costs were incurred and are recorded on a basis consistent with applicable generally accepted accounting principles, as amended from time to time. The Auditor also shall determine whether the amount of operating and maintenance expenses incurred in the wholesale division or allocated as outside-City expenses pursuant to this Agreement were allocated to the suburban purchasers in accordance with the methodology set forth in this Agreement.

(2) *Administrative and General Expenses.* The Auditor shall review the SFWD cost ledgers and other appropriate financial documents, including those of the SFPUC, to determine whether the recorded administrative and general expenses fairly reflect the costs incurred by or allocated to the SFWD and whether they are recorded on a basis consistent with applicable generally accepted accounting principles, as amended from time to time.

The Auditor also shall determine (a) whether the City overhead expenses and SFPUC charges were allocated to the SFWD in accordance with this Agreement and (b) whether the amount of administrative and general expenses allocated to the suburban purchasers was determined as provided by this Agreement.

(3) *Property Taxes.* The Auditor shall review the SFWD cost ledgers to determine whether the amount of property taxes recorded therein fairly reflects the property tax expense incurred by the City on behalf of SFWD property and whether there has been deducted from the amount to be allocated all taxes actually reimbursed to the City by tenants of SFWD property under leases that require such reimbursement.

The Auditor also shall determine whether the amount of property taxes to be allocated to the suburban purchasers was based on the methodology set forth in this Agreement.

(4) *Return on Rate Base.* The Auditor shall review such supporting documentation and utility plant ledgers as it deems necessary to determine whether: (1) changes in the rate base have been fairly reflected; (2) the cost of each asset has been assigned in accordance with Section 4.06 and/or Exhibit B of this Agreement; and (3) the debt percentage, the equity percentage, the return on debt, the return on equity, the overall rate of return and the suburban purchasers' share of return on rate base have been calculated in accordance with the methodology set forth in this Agreement.

(5) *Depreciation.* The Auditor shall review such supporting documentation and utility plant ledgers as it deems necessary to determine whether the total SFWD depreciation expense and the depreciation expense allocated to suburban purchasers were calculated in accordance with the methodology set forth in this Agreement.

(6) *Suburban Hetch Hetchy Assessment.* The Auditor shall determine whether the SFWD calculated the Suburban Hetch Hetchy Assessment in accordance with the principles set forth in this Agreement.

(A) *Operating and Maintenance Expenses, Administrative and General Expenses, Property Taxes.* The Auditor shall review the cost ledgers of the HHWPD and other appropriate

financial documents, including those of the SFPUC, to determine whether the expenses recorded fairly reflect the expenses incurred by or allocated to the HHWPD; whether expenses have been allocated among water-specific, joint, and power-specific categories in accordance with the methodology set forth in this Agreement; whether joint expenses have been reallocated to water and power in accordance with the methodology set forth in this Agreement; and whether water-related HHWPD expenses have been allocated to the suburban purchasers in accordance with the principles set forth herein.

(B) *Return on Rate Base.* The Auditor shall review such supporting documentation and utility plant ledgers as it deems necessary to determine whether (1) changes in the rate base have been fairly reflected, (2) the cost of each asset has been assigned in accordance with Section 4.08(a)(4)(i) and/or Exhibit H of this Agreement; and (3) the debt percentage, the equity percentage, the return on equity, the overall rate of return and the suburban purchasers' share of return on rate base have been calculated in accordance with the methodology set forth in this Agreement.

(C) *Depreciation.* The Auditor shall review such supporting documentation and utility plant ledgers as it deems necessary to determine whether the total HHWPD water related depreciation expense and the depreciation expense allocated to suburban purchasers were calculated in accordance with the methodology set forth in this Agreement.

(7) *Review of Contract Administration Costs.* The Auditor shall perform (1) a review of the supporting documentation used to determine the CPI adjustments provided for in Section 4.04 and (2) a review of the expenses charged to Account No. 6-49024 (Implementation and Administration of Suburban Settlement Agreement) to determine if these expenses were connected to the implementation or administration of this Agreement, taking into account the provisions of Section 4.04(c).

(8) *Review of Water Usage Rate Calculations.* The Auditor shall verify the mathematical accuracy of the calculations used by the City to derive the water usage rates defined in Exhibit J.

(d) *Use of and Reliance on Audited Financial Statements and Water Use Data.*

(1) In performing the audit, the Auditor shall incorporate any adjustments to the cost ledgers recommended by the independent accountant who has audited the financial statements of the SFPUC, SFWD and HHWPD as required by the Charter of the City. The Auditor may rely upon the work performed by that independent auditor if the Auditor reviews the work and is willing to take responsibility for it as part of the Auditor's audit.

(2) In performing the audit and issuing its report, the Auditor may rely on water use data furnished it by the SFWD, regardless of whether the suburban purchasers contest the accuracy of such data. The Auditor shall have no obligation to independently verify the accuracy of the water use data provided to it by the City; however, the Auditor shall disclose in its report any information in its possession which indicates that the water use data provided it by the City are inaccurate in any significant respect. Any error which would affect the City's calculation of the final surburban revenue requirement by one-half of 1 percent or more shall be deemed significant.

Section 6.05. *Issuance of Auditor's Report.*

The City will require the Auditor to issue its report no later than six months after the close of the fiscal year under audit.

The Auditor's report shall be addressed and delivered to the City and the Suburban Representatives and shall contain the following:

(1) An indentification of the material audited.

(2) A statement that the examination was made in accordance with generally accepted auditing standards.

(3) A description of the scope of the Auditor's work.

(4) An identification and description of the basis on which the material audited was prepared and of any variations between the basis on which it was prepared and the basis on which it should have been prepared.

(5) A description of any significant interpretations or assumptions regarding this Agreement made by the City in calculating the final suburban revenue requirement or by the Auditor in performing the audit.

(6) A statement whether or not in the Auditor's opinion (subject to the provisions of Section 6.04(d)(2)) the final suburban revenue requirement is fairly stated and has been calculated by the City in accordance with this Agreement and whether the amount posted by the City to the balancing account as a credit or charge to the suburban purchasers properly reflects the difference between the actual amounts paid by the suburban purchasers and the final suburban revenue requirement together with interest as provided for in Section 5.07(a). The Auditor shall also calculate the cumulative balance in the balancing account, after giving effect to the amount posted for the fiscal year under audit.

(7) A description of any significant changes in the City's accounting practices from the preceding year. Any change which would affect the City's calculation of the final suburban revenue requirement by one-half of 1 percent or more will be deemed significant.

(8) A statement whether or not, in the Auditor's opinion, the final suburban revenue requirement (for years after FY 1984/85) was prepared on a basis consistent with the preceding year.

(9) A statement whether, if the City has used estimated data in calculating the final suburban revenue requirement, the estimate was made in accordance with the requirements of Section 6.01(h).

Section 6.06. *Suburban Review.*

If the Suburban Representatives are not satisfied with the compliance audit conducted by the Auditor, the suburban purchasers shall have the right, at their own expense, to designate an auditor of their own ("the Suburban Auditor") to conduct a review ("the Suburban Review") of the Auditor's Report. The suburban purchasers shall reimburse the City for half of any overtime wages and related expenses paid by the City to its employees for time spent assisting or cooperating with the Suburban Auditor in connection with the suburban review.

The scope of the suburban review shall be limited to those portions of the Auditor's compliance report as are designated by the Suburban Representatives in a letter submitted by them or on their behalf to the General Manager of the SFWD, with copies to the Controller, the General Manager of the HHWPD, and the Auditor, within three months after receipt by the Suburban Representatives of the Auditor's compliance report. This designation shall be complete upon the receipt of said letter by the General Manager of the SFWD within the time indicated. If the Suburban Representatives designate only a portion of the Auditor's compliance report for review by the Suburban Auditor, and the Suburban Auditor's review of that portion causes the Suburban Auditor to believe that other portions of the Auditor's compliance report should be reviewed as well, the Suburban Representatives shall promptly designate such additional portions for further review by the Suburban Auditor by serving notice of such designation upon the General Manager of the SFWD and the Auditor. The Suburban Auditor shall have the right to review those portions of the City's records and the Auditor's working papers that are pertinent to the portions of the Auditor's compliance report that have been designated in accordance with this paragraph.

At the conclusion of the Suburban Auditor's review, representatives of the City and the Suburban Representatives shall meet to discuss any differences between them concerning the City's compliance with this Agreement during the previous year or the calculation of the previous year's final suburban revenue requirement. If such differences cannot be amicably resolved, the dispute shall be submitted to arbitration in accordance with Section 8.02 of this Agreement.

ARTICLE VII

WATER SUPPLY

Section 7.01. *Supply Assurance.*

The City agrees to supply water to the suburban purchasers as required, subject to a maximum annual average metered supply of water ("the Supply Assurance") equal to 184 million gallons per day (mgd), unless said amount is modified pursuant to the provisions of Section 2.01(d). This Supply Assurance shall be for the benefit of the suburban purchasers only, and no water sold by the City to any other person or entity (including, without limitation, any City departments or other entities associated with the City, wherever located, or any other water customer of City) shall be included within the Supply Assurance.

Notwithstanding the Supply Assurance established by this Section and the individual supply guarantees established by the presently-existing or recently-expired contracts between the City and the suburban purchasers and Section 7.02, the amount of water made available by the City to the suburban purchasers is subject to reductions, in accordance with Section 7.03, made necessary by reason of water shortage, drought, earthquakes, other acts of God, or rehabilitation or malfunctioning of the City's water delivery system, to the extent that and for the period that such events or circumstances prevent the City from fulfilling the Supply Assurance (including the individual guarantees) and the needs of the direct City water users. In the event of such a reduction, the City will restore its ability to fulfill the Supply Assurance (including the individual guarantees) and to meet the needs of direct City water users as soon as is reasonably practical.

The City agrees to use its best efforts to keep the SFWD and HHWPD water delivery system in good working order and repair. The City further agrees not to sell water to any resale or non-resale purchaser which is located outside the City's geographical limits and which was not purchasing water from the City on June 30, 1983, deliveries to which, either individually or in the aggregate, would impair the City's ability to fulfill the Supply Assurance. Tenants, lessees, and purchasers (and their successors in interest) of City property and City departments and agencies shall not be considered new purchasers within the meaning of this paragraph.

The Supply Assurance shall survive the termination of this Agreement and the Individual Contracts entered into pursuant hereto.

The parties acknowledge that the Supply Assurance is expressed in terms of daily deliveries on an annual average basis and does not itself constitute a guarantee by the City to meet peak daily or hourly demands of the suburban purchasers at the time their annual usage equals the Supply Assurance, irrespective of what those peak demands may be. The parties acknowledge, however, that the existing system has been designed and constructed to meet peak daily and hourly demands and that its capacity to do so has not yet been reached. The City agrees to operate the existing system to meet peak requirements of the suburban purchasers to the extent possible without adversely affecting its ability to meet peak demands of in-City customers. This Agreement is not intended to preclude the City from undertaking to meet specific peak demand requirements of individual suburban purchasers in the Individual Contracts.

Section 7.02. *Allocation of Supply Assurance.*

(a) The parties recognize that all the suburban purchasers have presently existing or recently-expired water supply contracts with the City and that certain, although not all, of these contracts contain provisions requiring the City to continue to supply the particular suburban purchaser with a specified amount of water after the expiration thereof unless and until a new contract between the City and the suburban purchaser is signed. The parties further recognize that two of these contracts (those between the City and the Alameda County Water District and between the City and the Dimond Public Utility District) contain supply guarantee provisions which fix the amount

of water guaranteed by the City by reference to water used during a calendar year (1984) not completed until after the effective date of this Agreement. Finally, the parties recognize that the contract between the City and the Estero Municipal Improvement District ("Estero") contains a supply guarantee provision which fixes the amount of water to be guaranteed by the City by reference to a year (2011) beyond the Term of this Agreement and that the contract between the City and the City of Hayward ("Hayward") does not contain an expiration date.

The intention of the parties to this Agreement is to preserve the entitlement of each suburban purchaser to the amount of water which it is or will be guaranteed by its presently existing or recently expired contract, that such guarantees shall continue to exist subsequent to the signing of this Agreement and the Individual Contracts, and that such guarantees (as they may be enlarged pursuant to Section 7.02(b)(3)) shall survive the expiration of this Agreement and the Individual Contracts.

Exhibit K-1, attached hereto, is a list which identifies the suburban purchasers (except Estero and Hayward) which shall be entitled to a specified quantity of water pursuant to this Section, by virtue of their existing contracts or this Agreement, and the quantity of water presently guaranteed to each. (The quantities set forth in Exhibit K-1 shall fix the present supply guarantee to each listed entity which becomes a party to this Agreement. However, neither those quantities nor the quantities set forth in Exhibit K-2 shall fix the present supply guarantee of any listed entity which does not become a party to this Agreement. The City and any such entity shall be free to use any relevant data (not including Exhibits K-1 and K-2) in determining the quantity of water to which such entity may be entitled under its existing or expired contract with the City.)

(b) The water entitlements guaranteed by the presently existing or recently expired contracts shall be included in the Supply Assurance. The Supply Assurance shall be allocated in the following manner:

First, the water used by Estero and Hayward shall, if each is a party to this Agreement, be subtracted from the Supply Assurance; the remainder shall be called the "suburban allocable water." (If Estero and/or Hayward is not a party to this Agreement, the Supply Assurance itself shall be periodically reduced as provided in Section 2.01(d); and the usage of whichever entity is not a party will not be subtracted from the Supply Assurance as so reduced.)

Second, the total amount of water presently set forth in Exhibit K-1 (127.55 mgd, subject to adjustment based on actual 1984 usage by Alameda County Water District and in the Dimond Public Utility District service area as described in Exhibit K-1) shall be subtracted from either (1) the suburban allocable water as defined by the preceding paragraph or (2) the Supply Assurance as adjusted in accordance with Section 2.01(d), whichever is applicable; the remainder produced by this subtraction shall be deemed "residual water". The residual water shall then be allocated as follows:

(1) If the suburban purchasers (other than Estero and Hayward) duly approve an allocation of some or all of the residual water, either unanimously or pursuant to a decision-making process previously ratified by the suburban purchasers, the City shall, upon reasonable notice of any such allocation, make reasonable efforts to apportion the residual water among the suburban purchasers in conformity therewith. The suburban purchasers shall notify the City of any allocation so approved by June 30 of each year, to be effective during the following fiscal year.

(2) If the suburban purchasers (other than Estero and Hayward) fail to notify the City by June 30, the City shall be entitled to assume that they have failed to approve an allocation (or further allocation) of residual water for the ensuing fiscal year. In any year as to which no allocation approved by suburban purchasers is in effect, the City shall deliver unallocated residual water to each individual suburban purchaser as it requires, (subject to the Supply Assurance) in accordance with its needs and then-existing service area. In delivering water to a suburban purchaser in accordance with this subsection, the City will incur no liability of any kind or character to any other suburban purchaser.

(3) If for three consecutive years the suburban purchasers fail to approve an allocation of some or all of the residual water, then the supply guarantees set forth in Exhibit K-1 will be deemed to be enlarged to the average amount of water used annually by each suburban purchaser during the three-year period (i.e., the sum of the usage in each year divided by 3). Each consecutive three-year period will be considered separately; the first such period will commence July 1, 1984 and end on June 30, 1987. In no event will the individual supply guarantees be reduced below the quantities presently set forth in Exhibit K-1.

(4) If both Estero and Hayward are parties to this Agreement and if the average use by suburban purchasers other than Estero and Hayward for one of the three-year periods defined in subsection (3), *supra,* exceeds the suburban allocable water, the enlarged individual supply guarantees of suburban purchasers other than Estero and Hayward will be reduced pro rata so that the total individual supply guarantees, as increased pursuant to subsection (3), *supra,* do not exceed the suburban allocable water. The pro rata reductions will be in accordance with the procedure set forth in Exhibit K-3.

If neither Estero nor Hayward is a party to this Agreement and if the average use by suburban purchasers for one of the three-year periods defined in subsection (3), *supra,* exceeds the Supply Assurance, as adjusted in accordance with Section 2.01(d), then the enlarged individual supply guarantees of suburban purchasers will be reduced pro rata so that the total individual supply guarantees, as increased pursuant to subsection (3), *supra,* do not exceed the adjusted Supply Assurance. The pro rata reductions will be in accordance with the procedure set forth in Exhibit K-3.

If either Estero or Hayward, but not both, is a party to this Agreement, the procedure described in this subsection 7.02(b) will apply *mutatis mutandis.*

The provisions of this subsection (4) are not in derogation of the reservation of claims to water in excess of the Supply Assurance contained in Section 7.04. Nor do they constitute an acknowledgment by suburban purchasers other than Estero and Hayward that the City is obligated or entitled to reduce their individual supply guarantees in the circumstance described herein. The provisions of this subsection (4) shall, however, govern the "vesting" procedure described in subsection (3), *supra,* unless and until a court determines that such provisions violate rights of the suburban purchasers derived independently of this Agreement. This paragraph is not intended to and shall not constitute a contractual commitment on the part of the City to furnish more than the Supply Assurance to the suburban purchasers or a concession by the City that the provisions of this subsection violate any rights of the suburban purchasers.

(5) At such time as the aggregate water usage of the suburban purchasers during a fiscal year is within 4 mgd of the Supply Assurance, the calculations described in subsections (3) and (4) shall be made as of the end of that fiscal year, and each year thereafter, rather than triennially and on an annual, rather than a three-year average, basis.

(c) It shall be the responsibility of each suburban purchaser to limit its water purchases from the City so as to comply with any allocation of the residual water made pursuant to this Section, regardless of whether such allocation has been approved by all the suburban purchasers (other than Estero and Hayward) pursuant to subsection (b)(1), established in accordance with subsection (b)(2), or derived through the procedure set forth in subsection (b)(3). The City shall in no event either be liable to any suburban purchaser or be obligated to supply more water to any suburban purchaser individually or to the suburban purchasers collectively than the amount otherwise allocated to it or them under this Agreement due to the use by any suburban purchaser of more water than the suburban purchaser is entitled to under this Agreement.

(d) The City shall install such new connections between the SFWD water system and that of any suburban purchaser that are necessary to deliver the quantities of water to which the suburban

purchaser is entitled under this Agreement. The City shall have the right to determine the location of such connections, in light of the need to maintain the structural integrity of the SFWD system and, where applicable, the need to limit peaking directly off the SFWD pipelines by individual suburban retail users of water, the need to ensure that suburban retail users of water have access to sufficient storage capacities in the appropriate suburban water system, the need to ensure that the suburban retail users of water have access to alternate sources of water in the event of a reduction in the City's ability to provide them with water, and other similar factors which may affect the desirability or undesirability of a particular location. The City's decisions regarding the location of new connections and the location, size and type of any new meters shall not be reviewable except for abuse of discretion or failure to provide the suburban purchasers with connections and meters adequate to deliver the quantities of water to which they are entitled under this Agreement.

Section 7.03. *Shortages.*

(a) Within six months after the effective date of this Agreement, the City and the suburban purchasers (who may act through the Suburban Representatives or other delegates) shall begin good faith negotiations to develop a "water conservation plan," which shall prescribe the steps which the City and the suburban purchasers shall take to encourage and require water conservation and to develop alternative sources of water in the event of a drought or other water shortage. The City and the suburban purchasers may agree to fund such studies as may be necessary to assist in the development of such plan, the expenses of which shall be borne one-half by the City and one-half by the suburban purchasers. The purpose of the negotiations shall be to arrive at a water conservation plan which allocates water between the City and the suburban purchasers and their retail customers in time of shortage. If a water conservation plan is adopted and approved by the City and by each of the suburban purchasers, the plan will supercede this provision and the provisions of subsection 7.03(b). The plan described in this subsection is not intended to be the urban water management plan required to be adopted by urban water suppliers under Sections 10610 *et seq.* of the Water Code unless all parties hereto subsequently agree as a part of the negotiations described herein.

(b) In the event that at any time during the Term of this Agreement there is not available in the SFWD and HHWPD water system sufficient water to supply the requirements of the suburban purchasers and the direct City water users, each suburban purchaser shall receive no more than that quantity of water which bears the same ratio to the total quantity of water then available in the City's water system, as the amount delivered to the suburban purchaser in the last preceding calendar year prior to the condition of shortage bears to the total amount delivered to all users supplied by the system during that calendar year.

(c) Nothing in this Agreement, including subsection (b), *supra,* shall be understood or construed as a concession by the City that it is required to allocate water between the suburban purchasers and the direct City water users during a water shortage on a pro rata basis, nor shall anything in this Agreement, including subsection (b), *supra,* waive or compromise the City's specifically-reserved claims that: (1) it is not required to allocate water between the suburban purchasers and the direct City water users in time of water shortage on a pro rata basis; (2) water used by the suburban purchasers in excess of the Supply Assurance may be disregarded in allocating water during times of water shortage; and (3) allocational methods other than pro rata reductions would allocate water between the suburban purchasers and the direct City water users during a water shortage more fairly and equitably than would pro rata reductions. Nothing in this Agreement, including subsection (b), *supra,* shall waive or compromise the suburban purchasers' denial of these claims or their specifically-reserved claim that the City has an obligation, derived independently from this Agreement, to allocate water between the suburban purchasers and the direct City water users in times of water shortage on a pro rata basis. In the event that an allocation of water is required at a time when the City and each suburban purchaser have not agreed on a water conservation plan pursuant to subsection (a), *supra,* the City shall allocate the available water

in the first instance and the suburban purchasers shall be free to challenge the allocation on any applicable legal or equitable basis.

(d) *Localized Water Reductions.* Notwithstanding the foregoing provisions of this Article, the City may reduce the amount of water available in or interrupt water deliveries to specific geographical areas within the SFWD's total service area to the extent that such reductions are necessary due to system emergencies, or in order to install, repair, rehabilitate, replace, investigate or inspect equipment in, or perform other maintenance work on, the SFWD and HHWPD water system. Such reductions or interruptions may be imposed by the City without corresponding reductions or interruptions in the amount of water available to SFWD water users outside the specific geographical area where reductions or interruptions are necessary, if the system's ability to supply water outside the specific geographical area has not been impaired. In the event of such a reduction or interruption, the City will restore the supply of water to the specific geographical area as soon as is reasonably practical. Except in cases of emergencies (during which oral notice shall be sufficient), the City will give the affected suburban purchaser(s) reasonable written notice of such localized reductions or interruptions, the reasons therefor, and the probable duration thereof. When the reduction or interruption is attributable to the scheduled installation, repair, rehabilitation, replacement, investigation or inspection of water delivery facilities, the City will use reasonable efforts to limit any such reduction or interruption in the delivery of water to the months of November through April.

Section 7.04. *Reservation of Claims to Additional Water; Service Area Expansion.*

(a) Nothing in this Agreement (including the Supply Assurance contained in Section 7.01 and the shortage allocation provisions contained in Section 7.03) is intended to or shall be construed to waive or compromise the potential or actual claim by any or all of the suburban purchasers that the City is obligated under federal or state law to supply it or them with water in addition to that guaranteed by Section 7.01 and allocated by Section 7.02 and/or to expand the City's existing water delivery system in order to furnish such additional water; nor shall anything in this Agreement (including Section 7.01) be construed to compromise or waive the City's denial of these claims.

(b) The suburban purchasers recognize that each Individual Contract does or will contain, as an exhibit, a map of their respective service areas. Any suburban purchaser which wishes to expand its service area shall notify the City, request the City's consent to the expansion, and provide information reasonably requested by the City regarding present and projected water demand within the area proposed to be added to the suburban purchaser's service area.

The foregoing provision is not intended to and shall not be construed to waive or compromise the potential or actual claim of any suburban purchaser (other than San Jose and Santa Clara whose service areas are fixed pursuant to Section 9.03) that the City is obligated under federal or state law to furnish water, included within the Supply Assurance, to them for delivery to customers outside their presently existing service areas and that they are entitled to enlarge their service areas to supply those customers with such water.

In order to assert any claims reserved by this subsection, however, a suburban purchaser must first have complied with the first paragraph hereof and its request must have either been refused by the City or not acted upon for six months after its submission to the City.

This section will not prevent the City and any suburban purchaser (other than San Jose and Santa Clara) from (1) agreeing in their Individual Contract or any amendment thereto that the suburban purchaser may expand its service area without subsequent City approval to a definite size but no larger and (2) waiving the provisions of this section with respect to any additional expansion. Nor shall this section prevent any suburban purchaser from (1) agreeing with the City in its Individual Contract or any amendments thereto that it will not expand its service area beyond

its present limits without City approval and (2) waiving the provisions of this section with respect to any additional expansion.

Section 7.05. *Restrictions on Resale.*

Each suburban purchaser agrees not to sell any water purchased from the City to any private party for resale by such private party to others, and further agrees not to sell any water from any source whatsoever to any private party for resale to others by substituting therefor water purchased from the City, without the City's prior written approval.

Each suburban purchaser also agrees that no water furnished by the City to it shall be delivered by it outside the service area described in an exhibit to its Individual Contract, and further agrees not to deliver any water outside the boundary of its service area by substituting therefor water purchased from the City, unless permitted by stipulation between the City and the suburban purchaser, or unless written consent for such delivery is entered into by the City and the suburban purchaser. The preceding sentence shall not apply to sales of water to another suburban purchaser on a temporary basis if the purchases of such water are authorized as emergency purchases under Section 7.07(a).

The City acknowledges that it has heretofore consented in writing to deliveries of water by individual suburban purchasers outside their service area boundaries and agrees that nothing in this Agreement is intended to affect such prior authorizations, which remain in full force and effect according to their terms. Such authorizations shall be identified in appropriate Individual Contracts. The City also agrees that it will not unreasonably withhold its consent to future requests by any suburban purchaser to deliver water to another suburban purchaser for resale.

Section 7.06. *Prohibition of Assignment.*

This Agreement is not for the benefit of any person, corporation, or other entity, other than the parties hereto, and no person, corporation or other entity except the parties hereto shall have rights or interests in or under this Agreement, except as expressly provided herein.

This Agreement shall be binding on, and shall inure to the benefit of, the parties to it and their respective successors and permitted assigns. Each suburban purchaser signing this Agreement agrees that it will not transfer or assign any rights or privileges under this Agreement, either in whole or in part, or make any transfer of all or any part of its water system or allow the use thereof in any manner whereby any provision of this Agreement will not continue to be binding on it, its assignee or transferee, or such user of the system. Any assignment or transfer in violation of this covenant, and any assignment or transfer that would result in the supply of water in violation of the Act, shall be void.

Nothing in this Section shall prevent any suburban purchaser (except the California Water Service Company, Cordilleras Mutual Water Association, and Stanford) from entering into a joint powers agreement or a municipal or multi-party water district with any other suburban purchaser (except those three listed above) to exercise the rights and obligations granted to and imposed upon the suburban purchasers hereunder, nor shall this Section prevent any suburban purchaser (except those three listed above) from succeeding to the rights and obligations of another suburban purchaser hereunder as long as the total service area served by the surburban purchasers involved in the succession is not thereby enlarged.

Section 7.07. *Prohibition of Water Purchases from Others; Use of Local Sources; Minimum Annual Purchases; Adjustment of Service Areas.*

(a) Each suburban purchaser, except for Alameda County Water District, and the Cities of Palo Alto, Sunnyvale, Mountain View, Milpitas, San Jose and Santa Clara, agrees that it will not, unless permitted by stipulation between it and the City, or unless given prior written approval of

such transaction by the City, contract for, purchase, or receive, with or without compensation either directly or indirectly, any water for delivery or use in each suburban purchaser's service area, from any person, corporation, or any entity whatsoever, whether public or private, including any governmental entity unless and until the suburban purchaser has demanded water from the City in accordance with the terms and conditions set forth herein and the City has refused to supply said additional water after due notice. In the event of such a request by any suburban purchaser and such a refusal by the City, the suburban purchaser(s) shall be free to purchase water from other entities, but only to the extent the City is unable and/or unwilling to supply the water needs of each such suburban purchaser. Nothing contained herein shall require any suburban purchaser to purchase water from the City over and above the water covered by the Supply Assurance, if the City is successful in its contention that the price for such additional water may legally include compensation to the City for decreased net power sale revenues resulting from the sale of such additional water. Nor shall anything contained herein prevent any suburban purchaser from purchasing water from sources other than the City, to the extent that such purchases are necessary to provide the suburban purchaser with water on an emergency and temporary basis. Each suburban purchaser who buys emergency water from any source other than the City shall give the City prompt notice of the nature of the emergency requiring such emergency purchases, the amount of water which is to be or has been purchased, and the duration of such purchases. The provisions of this subsection shall not apply to purchases of reclaimed wastewater in quantities up to twenty (20) percent of the amount of water which the suburban purchaser received from the City in calendar year 1981, as shown in Exhibit K-2. Purchases of reclaimed wastewater in any year in excess of that amount shall require approval by the City.

(b) The suburban purchasers shall use their best efforts to use all sources and supplies of water now owned or controlled by them, including all surface and ground water owned by the suburban purchasers within their respective service areas, to augment any supply demanded from the San Francisco Water Department, provided that water from such sources complies or can reasonably be made to comply with applicable state and federal drinking water quality standards or the water quality requirements of the suburban purchaser's commercial and industrial customers. Water which does not comply with applicable state and federal drinking water quality standards or meet the water quality requirements of commercial and industrial customers shall be used for other purposes by each suburban purchaser to the extent such use is economically and environmentally feasible. The suburban purchasers may acquire or develop wells, pumping plants or other sources of supply as necessary to supply water to their customers. (As used in the preceding sentence, "other sources of supply" does not include water purchased from suppliers other than the City.) The term "ground water" shall include all water available from aquifers within their respective service areas, whether such aquifers are recharged naturally or through artificial recharge facilities.

(c) Alameda County Water District and the Cities of Palo Alto, Sunnyvale, Mountain View, Milpitas, San Jose and Santa Clara shall be entitled to purchase water from sources other than the City; provided that the City may, in the case of San Jose and Santa Clara, and shall, in the case of each of the other entities, require that each purchase a minimum quantity of water from the City as a condition to this authorization. (If a suburban purchaser listed herein does not wish to have the right to purchase water from other sources without prior approval of the City, no minimum purchase requirements will be included in its Individual Contract.) These minimum required quantities will be contained in the Individual Contracts between the City and each suburban purchaser and will be expressed as minimum annual quantities which shall be no less than 80 percent and no more than 100 percent of the amount of water that particular suburban purchaser received from the City during calendar year 1981. Each of these Individual Contracts may also contain mutually acceptable monthly minimum and daily and hourly maximum water delivery levels; provided, however, that such maximum levels shall not be construed as allocations of residual water on an annual average basis and that, in the event of any conflict between the maximum daily and hourly levels and the

allocations of water provided for in Section 7.02 and 7.03 of this Agreement, the allocations shall control. Notwithstanding the preceding sentence, no water use which, taken on an annual basis, exceeds the amount obtained by multiplying the daily maximum by 365 shall vest for purposes of determining individual supply guarantees under the existing Individual Contracts or Section 7.02(b)(3).

The minimum purchase requirements in Individual Contracts will be waived during a drought or other period of water shortage if the water made available to the suburban purchaser is less than the minimum purchase quantity.

(d) If two or more suburban purchasers adjust the boundaries of their respective service areas so that one assumes an obligation to serve customers in an area that was previously within the service area of another suburban purchaser, they may also correspondingly adjust their Supply Guaranties as set out in Exhibit K-1 and the allocations of residual water under Section 7.02 between or among them.

Such adjustments shall require only the consent of the City and the suburban purchasers involved, so long as the Supply Assurance, the allocation of water to all other suburban purchasers, and the total service area of all suburban purchasers are not affected.

Any adjustment of service area boundaries that would result in the supply of water in violation of this Agreement or the Act shall be void.

ARTICLE VIII

OTHER AGREEMENTS OF THE PARTIES

Section 8.01. *Pricing of Additional Water.*

(a) The amounts to be paid by the suburban purchasers for water furnished to them within the Supply Assurance shall be governed by the rate-setting methodology described in Article IV. Should the City sell the suburban purchasers water in excess of the Supply Assurance, for whatever reason, pricing of that water ("additional water") will similarly be governed by the rate-setting methodology set forth in Article IV, subject to the City's explicitly reserved intention to add to such rates a surcharge that would reimburse the City for any decrease in the City's net power revenues which may directly or indirectly result from the sale of additional water to the suburban purchasers. As used in this Section, the term "net power revenues" means the revenues received by the City from the sale of electric power generated by facilities in the Hetch Hetchy system, less (1) the cost of generating the power and (2) the net revenues received by the City from the suburban purchasers for the additional water the sale of which allegedly gave rise to the decrease in power revenues. The suburban purchasers reserve the right to contest under any applicable provision of law both (1) the legality or propriety of any attempt by the City to include in the suburban revenue requirement a charge for decreased net power revenues allegedly resulting from the sale of additional water and (2) the amount of such decreased net power revenues, if any, in fact caused by the sale of additional water, and the methodology by which that amount is to be calculated. The suburban purchasers further reserve the right to contend that any surcharge which the City would otherwise be entitled to add to the rates charged for additional water pursuant to this Section may be partially or totally offset by a reduction in the rate paid for additional water if the City continues to contend that it has no obligation to provide such water to the suburban purchasers and such water is delivered to the suburban purchasers on an interruptible basis.

(b) Notwithstanding subsection (a), *supra,* no suburban purchaser shall contend that the rates charged for additional water should be less than those charged for water included within the Supply Assurance.

(c) With the exception of the issues explicitly reserved by subsection (a), no suburban purchaser shall contend, during the Term of this Agreement, that the suburban revenue requirements that result from the provision of such additional water as determined by this Section and Article IV violate any provision of federal law (including the Raker Act), state law, the Charter of the City and County of San Francisco, or any other provision of law. No resolution, judicial or otherwise, of any of the issues explicitly reserved by this Agreement (including the issues specifically reserved by this Section) shall affect in any way the suburban revenue requirements to be charged by the City for the provision of water covered by the Supply Assurance, as such suburban revenue requirements shall in all events be determined solely and exclusively by the rate-making methodology set forth in Article IV.

(d) The furnishing of additional water by the City to the suburban purchasers shall not be deemed or construed to be a waiver by the City of its claim that it has no obligation under any provision of law to supply such water to the suburban purchasers, nor shall it constitute a dedication by the City to the suburban purchasers of such additional water.

Section 8.02. *Arbitration and Judicial Review.*

(a) *Matters to be Arbitrated.* All questions or disputes arising under the following provisions of this Agreement shall be subject to mandatory, binding arbitration pursuant to the terms of this Section and shall not be subject to judicial determination:

(1) Section 3.04;

(2) All of Article IV;

(3) Sections 5.01, 5.06, and 5.07;

(4) All of Article VI;

(5) Section 8.03;

(6) Section 8.08 to the extent specified therein;

(7) Section 8.14(b); and

(8) Exhibits C, E and J.

All questions or disputes arising under Sections 5.02 and 5.03(a) shall be subject to either binding arbitration or judicial determination, as provided therein. Except as expressly provided to the contrary, all other questions or disputes arising under this Agreement (including, without limitation, those arising under Section 5.04) shall be subject to judicial determination.

(b) *Venue.* Any judicial action or proceeding arising under this Agreement shall be brought in the United States District Court for the Northern District of California or in the state courts of the State of California.

(1) If the action or proceeding ("action") is brought in state court, unless the parties to the action otherwise agree, the venue of such action shall be in the Superior Court in and for the County of Marin or any Municipal Court in the County of Marin, whichever court may have subject matter jurisdiction.

(2) If at the time the action is commenced in state court, or thereafter, the County of Marin or any public entity located therein is an actual or potential, direct or indirect, purchaser of water from the City, the following venue procedures shall apply instead of those set forth above in subparagraph (b)(1):

(A) If the action is one in which a jury is not of right, or trial by jury is waived, the action may be filed or maintained in the Superior Court or the Municipal Court for the County of Marin, but any party to the action may request the court to request the chairperson of the Judicial Council to assign a disinterested judge from a neutral county to hear the action and all proceedings in connection therewith pursuant to California Code of Civil Procedure Section 394(1).

(B) If the action is not one described in subparagraph (A), or if the chairperson of the Judicial Council does not assign a disinterested judge from a neutral county, then the action shall be commenced in, or if the action or proceeding has already been commenced in the Superior Court or any Municipal Court in the County of Marin it shall, on motion of any party, be transferred to, any court in the State of California, mutually agreed upon by the parties, having subject matter jurisdiction and located in any county other than Alameda, San Mateo, San Francisco, or Santa Clara counties. In the absence of such agreement, any such state court action or proceeding shall be commenced in or transferred on motion of any party to any court in the State of California having subject matter jurisdiction and located in any county other than Alameda, San Mateo, San Francisco, or Santa Clara counties.

(c) *Demand For Arbitration.* If any arbitrable question or dispute should arise, any suburban purchaser or the City may commence arbitration proceedings hereunder by service of a written Demand for Arbitration. All Demands shall set forth the issues to be arbitrated and the general contentions relating to those issues of the party serving the Demand. Within 45 days after service of a Demand upon it, any suburban purchaser or the City may serve a Notice of Election to become a party to the arbitration and a Response to the Demand, setting forth its position and general contentions with respect to the issues set forth in the demand. If a timely Notice of Election and Response is not filed by any such entity, it shall not be a party to the arbitration, but shall nonetheless be bound by the award of the arbitrator pursuant to Section 8.02(g)(10). If no party to this Agreement serves a timely Notice of Election and Response, the party seeking arbitration

shall be entitled to the relief sought in its Demand for Arbitration without the necessity of further proceedings.

If a Demand or Notice of Election is made by the City, it shall be served by personal delivery or certified mail to each suburban purchaser at the address of such purchaser as set forth in the billing records of the San Francisco Water Department at such time. If a Demand or Notice of Election is made by a suburban purchaser, service shall be by certified mail or personal delivery to the General Manager, San Francisco Water Department, 425 Mason Street, San Francisco, California 94102, and to each of the other suburban purchasers. If arbitration is commenced, the suburban purchasers shall use their best efforts to formulate a single, joint position with respect thereto. In any event, with respect to the appointment of arbitrators, as hereinafter provided, all suburban purchasers that take the same position as to the issues to be arbitrated shall jointly and collectively be deemed to be a single party.

(d) *Limitations Period.* All Demands For Arbitration shall be served within four years of the date on which the cause of action arose, provided that no amount posted to the balancing account by the City pursuant to Section 5.07 for any individual fiscal year shall be adjusted thereafter in any respect (except by agreement of the City and the Suburban Representatives) unless a Demand seeking such relief is served within eighteen months of receipt by the Suburban Representatives of the Auditor's Report for that year as provided in Section 6.05. (If the Suburban Representatives receive the Report on different days, then the date of receipt for purposes of this subsection shall be the date the Report is received by the Suburban Representative which purchased the largest quantity of water from the City during the fiscal year which the Report concerns.) If no such Demand is served within the eighteen month period specified above, the amount posted to the balancing account for that year shall be deemed final and conclusive.

An adjustment in the balancing account resulting in an award based on a timely Demand shall not be precluded merely because the cumulative balance in the balancing account to which the adjustment is to be made is comprised in whole or in part of amounts posted to the balancing account that have become final in accordance with this subsection, provided, however, that in no event shall there be any adjustment of amounts so posted which have become final in accordance with this subsection.

The Arbitrator may order the alteration or recalculation of underlying SFWD and/or HHWPD accounts or asset classifications that will be used to determine future suburban revenue requirements, even though the existing entries in such accounts or the asset classifications, in whole or in part, predate the four-year and eighteen-month periods described above, so long as a timely arbitration demand has been filed in accordance with this subsection.

(e) *Number And Appointment Of Arbitrators.* All arbitration proceedings under this Section shall be conducted by a single arbitrator, selected by the City and a designated representative of the suburban purchasers or each group of suburban purchasers that take the same position with respect to the arbitration within 75 days after service of the demand for arbitration. If the parties to the arbitration cannot agree on an arbitrator within 75 days, any party may petition the Superior Court in and for the County specified in Section 8.02(b), for the appointment of an arbitrator.

(f) *Guidelines For Qualifications Of Arbitrators.* The suburban purchasers and the City acknowledge that the qualifications of the arbitrator will vary with the nature of the matter arbitrated, but, in general, agree that such qualifications may include expertise in one or more of the following fields: water utility rate setting, water system and hydraulic engineering, utility accounting methods and practices, and water system operation and management. The parties to the arbitration shall use their best efforts to agree in advance upon the qualifications of any arbitrator to be appointed by the Superior Court.

(g) *Powers of Arbitrator; Conduct of Proceedings.*

(1) Except as hereinafter provided, arbitrations under this Section 8.02 shall be conducted under and be governed by the provisions of California Code of Civil Procedure, Sections 1282.2 through 1284.2 (hereinafter, collectively, "Code sections"), and arbitrators appointed hereunder shall have the powers and duties specified by the Code sections.

(2) Within the meaning of the Code sections, the term "neutral arbitrator" shall mean the single arbitrator selected by the parties to the arbitration.

(3) Unless waived in writing by the parties to the arbitration, the notice of hearing served by the arbitrator shall not be less than 90 days.

(4) The lists of witnesses (including expert witnesses), and the lists of documents (including the reports of expert witnesses) referred to in Code of Civil Procedure Section 1282.2 shall be mutually exchanged, without necessity of demand therefor, no later than 60 days prior to the date of the hearing, unless otherwise agreed in writing by the parties to the arbitration.

(5) The time for making the award shall be no later than 18 months after service of the initial demand for arbitration, provided that such time may be waived or extended as provided in Code of Civil Procedure Section 1283.8.

(6) The arbitrator shall not base his or her award on information not obtained at the hearing.

(7) The provisions for discovery set forth in Code of Civil Procedure Section 1283.05 are incorporated into and made part of this Agreement, except that: (a) leave of the arbitrator need not be obtained for the taking of depositions, including the depositions of expert witnesses; (b) the provisions of Code of Civil Procedure Section 2037 *et seq.,* relating to discovery of expert witnesses, shall also be applicable to arbitration proceedings arising under this Agreement, except that the time period set forth in Section 2037(a) shall be deemed to be not later than 60 days prior to the date for the hearing; and (c) all reports, documents, and other materials prepared or reviewed by any expert designated to testify at the arbitration shall be discoverable. In appropriate circumstances, the arbitrator may order any party to this Agreement that is not a party to the arbitration to comply with any discovery request.

(8) For the purposes of allocation of expenses and fees, as provided in Code of Civil Procedure Section 1284.2, if any two or more suburban purchasers join together in a single, joint position in the arbitration, those suburban purchasers shall be deemed to be a single party. If any suburban purchaser or purchasers join together with the City in a single joint position in the arbitration, those suburban purchasers and the City together shall be deemed to be a single party.

(9) The arbitrator shall have the power to issue orders mandating compliance with the terms of this Agreement or enjoining violations of this Agreement subject to the limitations contained herein and in Section 8.02(d). The powers of the arbitrator, with respect to any arbitration brought to redress a claimed suburban overpayment to the City, shall be limited to entering an order requiring that an adjustment be made in the amount posted to the balancing account (if not prohibited by Section 8.02(d)) or either or both of the orders described in Section 5.07(d), if appropriate under Section 5.07(d).

(10) All awards of the arbitrator shall be binding on the City and the suburban purchasers regardless of the participation or lack thereof by any suburban purchaser or the City as a party to the arbitration proceeding.

Section 8.03. *Special Provisions re Attorneys' Fees.*

(a) Each party will bear its own costs, including attorneys' fees, incurred in any arbitration or litigation arising under this Agreement or the Individual Contracts between the City and the

suburban purchasers. Notwithstanding the foregoing, the City may partly allocate to the suburban purchasers as an allowable expense under Article IV (utilizing the composite rate used for allocating other SFWD administrative and general expenses) any costs or fees incurred by the City in connection with arbitration and/or litigation arising under this Agreement and/or the Individual Contracts, except that any and all costs incurred by the City through the use of attorneys other than the San Francisco City Attorney's Office in arbitration and/or litigation arising under this Agreement and/or the Individual Contracts shall not be allocable to the suburban purchasers.

(b) If, in any litigation and/or arbitration between the parties not arising under this Agreement or the Individual Contracts but involving the respective rights and obligations of the parties *vis-a-vis* the City's Hetch Hetchy system, or water delivered therefrom (including, without limitation, litigation and/or arbitration concerning the issues specifically reserved by Sections 2.04, 5.05, 7.04, 8.01, 8.08 and 9.03(c) of this Agreement), the costs, including attorneys' fees, are awarded to the suburban purchasers, the payment of those costs and fees by the City will not be deemed an allowable expense under Article IV. If no such award is made, the City's costs and/or fees shall be allocated between the City and the suburban purchasers pursuant to this Agreement, utilizing the composite rate used for allocating other SFWD administrative and general costs. Any award to the City of fees and costs incurred in connection with such an action shall be reduced to offset the amount of the City's fees, if any, which have already been borne by the suburban purchasers pursuant to the allocation procedures set forth herein.

(c) Nothing contained in this Agreement shall require the City to change retroactively its allocation of the action's litigation costs and attorneys' fees incurred prior to the beginning of the Agreement's Term.

(d) Except as provided in subparagraphs (a) and (b), *supra*, all attorneys' fees and costs incurred by the City in connection with the operation and maintenance of the City's water supply system shall be allocated between the City and the suburban purchasers utilizing the applicable rate under Section 4.04(c).

Section 8.04. *Suburban Advisory Group.*

The parties wish to insure that the suburban purchasers may, in an orderly way, be informed of matters affecting the SFWD water system, including matters affecting the continuity and adequacy of their water supply from the City. To that end, each suburban purchaser may nominate one representative to a Suburban Advisory Group ("Group"). The City shall, through the General Manager of the SFWD and the General Manager of the HHWPD, meet with the Group (or with a subcommittee selected by the Group) semiannually, at mutually convenient times. The General Manager of the SFWD and the General Manager of the HHWPD may designate an appropriate official of their respective departments if, for illness or other reasons beyond their control, they are unable to attend. The first such meeting shall be held, if requested, no later than three months after the effective date of this Agreement. The City shall, at such meetings, provide the Group or its representatives with information on the following topics, to the extent such information is available to the City:

(a) Any capital additions being considered or planned for the SFWD and HHWPD, including the status of planning studies, financing plans, permit applications, environmental reviews, etc.;

(b) Water supply and usage trends and projections for the City, direct City water users, and the suburban purchasers, including the Commercial Division monthly reports which have been prepared by the City since the last meeting held pursuant to this Section;

(c) The status of administrative proceedings and litigation affecting the water rights to the HHWPD and SFWD sources of supply; and

(d) Existing or anticipated problems with the maintenance and repair of the water delivery system and water quality.

Additional topics shall be included on the agenda of a meeting at the request of the Suburban Representatives, provided that the City is notified of the topic no less than ten days in advance of the meeting. If the Suburban Representatives wish to inspect any documents relating to any topic on the agenda of a meeting, they shall request the City to produce such documents at the meeting no less than ten days in advance thereof. The City shall make reasonable efforts to comply with such requests for documents.

The meetings provided for by this Section are in addition to the meeting addressed to the SFWD and HHWPD budget provided for by Section 5.02, but the budget meeting and one of the meetings provided for herein may be held *seriatim,* if that is mutually convenient.

Additional meetings between the Group and the City may be held upon the request of either the City or a majority of the Group's members, provided that the General Managers of the SFWD and HHWPD shall not be obligated to attend such meetings.

Section 8.05. *Notice of Water Rights Proceedings.*

The City shall use its best efforts to give prompt notice to the suburban purchasers of any litigation or administrative proceedings to which the City is a party involving water rights to the SFWD and HHWPD sources of supply. The City's failure to provide notice as required by this Section, for whatever reason, shall not give rise to any monetary liability.

Section 8.06. *Notice.*

Except for (1) the materials which the City is required to mail to the Suburban Representatives pursuant to Sections 5.02, 5.03(a), 6.01, 6.04 and 8.11 and (2) the counterpart of this Agreement which the City is required to mail to the San Francisco Bay Area Water Users Association ("BAWUA") pursuant to Section 8.10, all notices and other documents which the City is required or permitted to send to the suburban purchasers under this Agreement shall be sent to each and all of the suburban purchasers by United States mail, first class postage prepaid, addressed to each suburban purchaser at the address to which monthly water bills are mailed by the SFWD.

All notices or other documents which the suburban purchasers or the Suburban Representatives are required or permitted to send to the City under this Agreement shall be sent by United States mail, first class postage prepaid, addressed as follows:

General Manager
San Francisco Water Department
425 Mason Street
San Francisco, CA 94102

Each suburban purchaser is a member of BAWUA, a California unincorporated association. The City shall send a copy of each notice or other document which it is required to send to all suburban purchasers or to the Suburban Representatives to BAWUA addressed as follows:

San Francisco Bay Area Water Users Association
c/o Belmont County Water District
P.O. Box 129
Belmont, CA 94002

The failure of the City to send a copy of such notices or documents to BAWUA shall not invalidate any rate set or other action taken by the City.

Any party (or BAWUA) may change the address to which notice is to be sent to it under this Agreement by notice to the City (in the case of a change desired by a suburban purchaser or BAWUA) and to the suburban purchasers and BAWUA (in the case of a change desired by the City).

The requirements of notice set forth in Section 8.02 concerning arbitration shall prevail over this Section, when they are applicable.

Section 8.07. *Rates Applicable to Other Resale Users.*

Notwithstanding any other provision of this Agreement, the City will not voluntarily provide water to any resale customer which is located west of Irvington Portal and which is not a party hereto at rates which are lower than those determined under Article IV and Section 8.01 without making such rates applicable to the suburban purchasers.

Nothing in this Section shall require the City to lower its rates to the suburban purchasers if the rate differential between the rates charged the suburban purchasers and the rates charged to resale customer(s) which are located west of Irvington Portal and which are not parties to this Agreement results (a) from a court order resulting from litigation between the City and the resale customer or the settlement of such litigation; (b) from a court order resulting from litigation between the City and another resale customer who is similarly situated or the settlement of such litigation; (c) from a court order resulting from litigation between the City and the United States (or any department or official thereof) or the settlement of such litigation; or (d) from rate structure(s) for the suburban purchaser(s) which are based upon the quantity of water used and which are designed either to discourage the use by the suburban purhasers of, or to allocate a surcharge under Section 8.01 imposed on, additional water. Nothing in this Section shall be construed as or is intended to be a concession by the suburban purchasers that the City is entitled to adopt such a rate structure or impose such a surcharge.

Section 8.08. *Changes in the City's Water Delivery System.*

The parties contemplate that, over the Term of this Agreement, the City may expand the capacity of its existing water delivery system through additions to the system and/or the replacement of existing assets. In the event such an expansion of capacity occurs, or in the event that new assets are added to the system without expanding the system's capacity, questions may arise concerning the proper classification of such new assets within the categories into which the SFWD and HHWPD rate bases are divided by this Agreement.

The parties also contemplate that, in connection with such expansion of system capacity, the City may offer to increase the Supply Assurance to the suburban purchasers set out in Section 7.01. In the event that the City offers to provide the suburban purchasers with such an increased guarantee and the suburban purchasers accept the offer, questions may arise concerning the respective City and suburban shares in the ultimate capacity of the system.

The parties shall have an obligation as to all such questions to negotiate in good faith, and if agreement between the parties is not reached, the matter shall be referred to arbitration pursuant to Section 8.02. As part of such negotiations, the parties may agree to fund studies of system capacity and usage and/or new assets by consultants selected jointly by the City and the Suburban Representatives. The expenses of any such study shall be borne one-half by the City and one-half by the suburban purchasers. Nothing in this Section shall prevent the City from unilaterally initiating studies of system capacity and usage and/or new assets by consultants of its choice and allocating the cost of such studies in accordance with the other provisions of this Agreement.

Nothing in this Agreement shall be construed to impose any obligation on the City to expand its existing water delivery system for the benefit of the suburban purchasers or to deliver to the suburban purchasers more water than that contained in the Supply Assurance set out in Section 7.01 nor shall anything herein be deemed to be a waiver of any claims by the suburban purchasers that the City has an obligation, independent of this Agreement, to do so.

Section 8.09. *Representations During Settlement Negotiations.*

During the course of settlement negotiations, the parties have exchanged various computer printouts and other materials which contain projections of the likely effect of this settlement on the suburban revenue requirement. The parties acknowledge that these projections are merely predictions by their consultants as to future events and that such projections are necessarily uncertain. Each party signing this Agreement therefore releases all other parties to this Agreement, and each other party's lawyers and expert accounting and engineering consultants, from any and all liability arising from the sharing of projections, computer printouts, or any other representations as to the likely effect of this Agreement. Each party signing this Agreement has been fully advised by its attorneys, and their accounting and engineering experts, on the contents of this Agreement and its legal effects.

Section 8.10. *Counterparts.*

Execution of this Agreement may be accomplished by execution of separate counterparts by each signatory. The City shall deliver its executed counterpart to the Bay Area Water Users Association and the counterpart which each suburban purchaser executes shall be delivered to the City. The separate executed counterparts, taken together, shall constitute a single agreement. When this Agreement becomes effective pursuant to Section 2.01, the City shall provide any suburban purchaser that so requests a counterpart original of this Agreement signed on behalf of the City.

Section 8.11. *SFWD Rules and Regulations.*

The sale and delivery of all water hereunder shall be subject to such of the "Rules and Regulations Governing Water Service to Customers" of the SFWD adopted by the SFPUC, as those Rules and Regulations may be amended from time to time, as are (1) applicable to the sale and delivery of water to the suburban purchasers, (2) reasonable, and (3) not inconsistent with either this Agreement or with an Individual Contract.

The City will give the Suburban Representatives notice of any proposal to amend the Rules and Regulations in a manner which would affect the suburban purchasers. The notice will be delivered at least thirty days in advance of the date on which the proposal is to be considered by the SFPUC and will be accompanied by the text of the proposed amendment.

Section 8.12. *Preservation of Water Rights.*

It is the intention of the City to preserve all of its water rights, whether or not the water to which the City presently holds water rights is allocated under this Agreement. Nothing in this Agreement shall be construed as an abandonment by the City, or an intention by the City to abandon, any of the water rights that it presently possesses.

Section 8.13. *Suburban Representatives.*

As used in this Agreement, the term "Suburban Representatives" shall mean the five suburban purchasers selected by the suburban purchasers as a group to exercise the rights granted to and fulfill the obligations imposed upon the Suburban Representatives by this Agreement. If the suburban purchasers fail to select Suburban Representatives, the Suburban Representatives shall be the five suburban purchasers which purchased the largest quantity of water during the prior fiscal year. The suburban purchasers shall promptly notify the City of any changes in the Suburban Representatives whom they have selected and the City shall be entitled to assume that the Suburban Representative(s), once selected by the suburban purchasers or chosen pursuant to this Section, shall continue in that role, until the City receives information of any such change.

Section 8.14. *Reservation of Claims Regarding Suburban Purchase of Water From In-City Retail Distribution System.*

(a) Nothing in this Agreement shall prevent the City and any suburban purchaser from providing by contract that the City may charge rates which are higher than those which would otherwise be proper under this Agreement for water delivered by the City to the suburban purchaser through transmission and distribution lines and mains in the in-City retail distribution system (i.e., transmission mains and distribution lines located within the City's geographical limits other than those which deliver water from Hetch Hetchy and local sources to Sunset, University Mound, and Merced Manor Reservoirs). Nothing in this Agreement shall be construed to waive or compromise the City's claim that it is entitled to charge such higher rates for water delivered through the in-City retail distribution system or the suburban purchasers' denial of such claim. Nothing in this Agreement shall obligate the City to supply any suburban purchaser with water delivered through the in-City retail distribution system.

(b) Any water delivered by the City to any suburban purchaser through the in-City retail distribution system and paid for at rates which are greater than those which would otherwise be proper under this Agreement shall be counted as City usage for the purpose of determining the ratios used to allocate assets and expenses pursuant to this Agreement.

The City has, prior to the Term of this Agreement, provided a portion of the water it delivers to Daly City through two connections to its in-City retail distribution system located within the City's boundaries. The parties hereto recognize that the Individual Contract between the City and Daly City will provide for the continuation of this arrangement under the mutually acceptable terms, conditions and limits set forth therein. This Individual Contract will also provide that water delivered by the City to Daly City through these two connections shall be billed at the same rates as water delivered to the other suburban purchasers. No party hereto will contend that the continuation of this arrangement as provided in the City-Daly City Individual Contract is a precedent for or otherwise obligates the City to furnish it water through the in-City retail distribution system or, if water is so furnished, to charge for such water only at rates otherwise proper under this Agreement. The provisions of the preceding sentence shall apply to Daly City insofar as additional in-City connections, or enlargements of the existing meters and services, are concerned.

Section 8.15. *Expenses Chargeable to Individual Suburban Purchasers.*

The expenses associated with the following services shall be directly chargeable to and payable by the individual suburban purchaser for which the service is rendered and shall not be chargeable to the suburban purchasers generally under Article IV:

(a) installation of meters and service connections;

(b) relocation of meters and service connections;

(c) enlargement of meters and service connections;

(d) removal of meters and service connections; and

(e) modification of meters and service connections as requested by an individual suburban purchaser.

Section 8.16. *Incorporation of Exhibits.*

Exhibits A through O, referred to herein, are incorporated in and made a part of this Agreement.

Section 8.17. *Actions and Approvals by the City.*

Whenever City action or approval is required or contemplated by this Agreement, authority to act or approve shall be exercised by the SFPUC or its designee, except if such action or approval is required by law to be taken or given by the City's Board of Supervisors.

Section 8.18. *Filing of Notices.*

Within five days after the effective date of this Agreement, the City shall file a Notice of Exemption, in the form provided for by 14 Cal. Admin. Code Section 15062, with the County Clerks of the City and County of San Francisco and the Counties of San Mateo, Santa Clara and Alameda. If the City fails to file the notices in the time and manner provided for herein, then the Plaintiffs, or any of them, are authorized to do so on behalf of the City. In the event any action or proceeding is filed against any party to this Agreement attacking the validity of the determination underlying the Notice, any other party to this Agreement may be joined as a defendant or respondent therein by motion of the party named in the action or proceeding and agrees not to oppose such joinder.

Section 8.19. *Section Headings.*

The marginal headings and titles to the sections and paragraphs of this Agreement are not a part of this Agreement and shall have no effect upon the construction or interpretation of any part hereof.

ARTICLE IX

IMPLEMENTATION AND SPECIAL PROVISIONS AFFECTING CERTAIN SUBURBAN PURCHASERS

Section 9.01. *General.*

As described in Section 7.02, the City previously entered into water supply contracts with each of the suburban purchasers, typically for terms of 20 years. The initial terms of the majority of those contracts have now expired and, except as provided below, the suburban purchasers will execute new water supply contracts with the City concurrently with their approval of this Agreement. These Individual Contracts will describe the service areas of each suburban purchaser, identify the size and location of connections between the SFWD transmission system and the suburban purchaser's distribution system, provide for periodic rendering and payment of bills for water usage, and in some instances, contain additional specialized provisions unique to each purchaser and not of general concern or applicability. A sample of the Individual Contract to be entered into is attached as Exhibit L. The Individual Contracts between the City and the suburban purchasers will not contain any provisions inconsistent with Articles I through VIII of this Agreement, except: (1) as provided below in this Article; or (2) to the extent that such provisions are not in derogation of the rights that other suburban purchasers have under this Agreement and their Individual Contracts. Any provisions in an Individual Contract which are in violation of this Section shall be void.

Section 9.02. *California Water Service Company.*

The parties recognize that the California Water Service Company, one of the suburban purchasers, is a private, for-profit corporation and, as such, has no claim to co-grantee status under the Act, which specifically bars private parties from receiving for resale any water produced by the City's Hetch Hetchy system or otherwise subject to the Raker Act. The parties also recognize that the California Water Service Company is a member of the Bay Area Water Users Association, the entity which has coordinated Plaintiffs' maintenance of the action, and that the suburban purchasers have insisted upon the inclusion of the California Water Service Company as a party to this Agreement as a precondition for their own acquiescence hereto. Accordingly, the following provisions shall apply to the California Water Service Company, anything to the contrary elsewhere in this Agreement notwithstanding:

(a) The total quantity of water delivered by the City to the California Water Service Company shall not in any calendar year exceed 47,400 acre feet, unless through improvements in the City's local production facilities in Santa Clara, Alameda, San Mateo, or San Francisco Counties, made after August 21, 1961 (the date of the previous contract between the City and California Water Service Company) the City develops or has developed additional local sources in those counties, in which event the maximum stated herein may be increased by the City, upon determination by it of the need by California Water Service Company for water service in excess of the maximum stated herein. Such an increase shall automatically increase the Supply Assurance commitment to the suburban purchasers collectively (including the California Water Service Company) by an equivalent amount, but only if it is based on development of additional local sources after the effective date of this Agreement. It is agreed that the City has no obligation to deliver water to California Water Service Company in excess of the maximum stated herein, except as such maximum may be increased by the City pursuant to this subsection. Nothing in this Agreement shall preclude the City from selling water to any county, city, town, district, political subdivision, or other public agency for resale to customers within the service area of the California Water Service Company. The maximum annual quantity set forth in this subsection is intended to be a limitation on the total quantity of water that may be allocated to California Water Service Company; it is not itself intended to serve as an allocation of water under Section 7.02.

(b) Nothing in this Agreement shall require or contemplate any delivery of water to California Water Service Company in violation of the Act, which statute imposes certain obligations upon the City as a grantee from the United States in regard to the disposal of water and electricity from the Hetch Hetchy project.

(c) Nothing in this Agreement shall alter, amend or modify the Findings of Fact and Conclusions of Law and the Judgment dated May 25, 1961, in that certain action entitled *City and County of San Francisco v. California Water Service Company* in the Superior Court of the State of California in and for the County of Marin, No. 23286, as modified by the Quitclaim Deed from California Water Service Company to the City dated August 22, 1961. The rights and obligations of the City and California Water Service Company under these documents shall continue as therein set forth.

(d) Notwithstanding anything in Section 7.06 to the contrary, California Water Service Company shall have the right to assign to a public agency having the power of eminent domain all or a portion of the rights of California Water Service Company under any contract between it and the City applicable to any individual district of California Water Service Company in connection with the acquisition by such public agency of all or a portion of the water system of California Water Service Company in such district. In the event of any such assignment of all the rights, privileges and obligations of California Water Service Company under such contract, California Water Service Company shall be relieved of all further obligations under such contract provided that the assignee public agency expressly assumes the obligations of California Water Service Company thereunder. In the event of such an assignment of a portion of the rights, privileges and obligations of California Water Service Company under such contract, California Water Service Company shall be relieved of such portion of such obligations so assigned thereunder provided that the assignee public agency shall expressly assume such obligations so assigned to it.

Section 9.03. *City of San Jose and City of Santa Clara.*

The suburban purchasers recognize that the City has in the past provided water to the City of San Jose ("San Jose") and the City of Santa Clara ("Santa Clara") on a temporary and limited basis. In light of this fact, certain provisions of this Agreement shall be inapplicable to San Jose and Santa Clara, in the following respects:

(a) *City of San Jose.* The City's last agreement with San Jose expired on June 30, 1982. Water delivered to San Jose by the City between July 1, 1982 and July 31, 1983 shall be charged by the City and paid for by San Jose at the City's water rates which were in effect prior to July 31, 1983. From August 1, 1983 through June 30, 1985, the City will furnish water to San Jose at the same rates as those applicable to other suburban purchasers pursuant to this Agreement. On or before July 1, 1985, the City will exercise one of the following options with respect to its continuing water service to San Jose after that date.

(i) The City may elect to take on San Jose as a permanent customer, subject to minimum and maximum water delivery levels to be negotiated between the City and San Jose, provided that San Jose's service area and maximum annual usage during the balance of the Term of this Agreement shall not exceed those shown in Exhibit M. If the City so elects and San Jose accepts this offer: (1) San Jose will pay for water in accordance with the methodology set forth in this Agreement, such rates to be identical to those charged the other suburban purchasers; (2) water delivered to San Jose shall be included within the Supply Assurance; (3) San Jose will be entitled to a supply guarantee (to be included within the Supply Assurance) based on its usage during calendar year 1981 (500,239,960 gallons); and (4) its share of residual water will be determined in accordance with Section 7.02.

(ii) Alternatively, the City may continue to sell water to San Jose on a temporary and, after June 30, 1987, interruptible basis, but at rates identical to those charged other suburban

purchasers. If the City continues to provide water to San Jose on a temporary and, after June 30, 1987, interruptible basis, the amount of water furnished to San Jose shall not be included within the Supply Assurance. The City will provide at least two years notice to San Jose prior to termination of service, and the water delivered to San Jose after June 30, 1987, shall be limited by the City's ability to meet the full needs of all its other water customers (including in-City residents and other direct City water users). Delivery of water to San Jose may be subject to minimum and maximum water delivery levels, which will be negotiated between the City and San Jose, provided that San Jose's service area and maximum annual usage shall not exceed that set forth in Exhibit M.

(iii) Finally, the City may elect to terminate its water service to San Jose. If the City elects to exercise this option, it shall notify San Jose of its intention to do so no later than July 1, 1985, and the termination of service shall occur no earlier than July 1, 1987.

(b) *City of Santa Clara.* The City's existing contract with Santa Clara expires on June 30, 1984. From July 1, 1984 through June 30, 1985, the City shall furnish water to Santa Clara on the same rates as those applicable to other suburban purchasers pursuant to this Agreement. On or before July 1, 1985, the City will exercise one of the following options with respect to its continuing water service to Santa Clara after that date.

(i) The City may elect to take on Santa Clara as a permanent customer, subject to maximum and minimum water delivery levels to be negotiated between the City and Santa Clara, provided that Santa Clara's service area and maximum annual usage during the balance of the Term of this Agreement shall not exceed those shown in Exhibit M. If the City so elects and Santa Clara accepts this offer: (1) Santa Clara will continue to pay for water in accordance with the methodology set forth in this Agreement, such rates to be identical to those charged the other suburban purchasers; (2) water delivered to Santa Clara shall be included within the Supply Assurance; (3) Santa Clara will be entitled to a supply guarantee (to be included within the Supply Assurance) based on its usage during calendar year 1981 (633,810,320 gallons); and (4) its share of residual water will be determined in accordance with Section 7.02.

(ii) Alternatively, the City may continue to sell water to Santa Clara on a temporary and, after June 30, 1987, interruptible basis, but at rates identical to those charged other suburban purchasers. If the City continues to provide water to Santa Clara on a temporary and, after June 30, 1987, interruptible basis, the amount of water furnished to Santa Clara shall not be included within the Supply Assurance. The City will provide at least two years notice to Santa Clara prior to termination of service, and the water delivered to Santa Clara after June 30, 1987, shall be limited by the City's ability to meet the full needs of all its other water customers (including in-City residents and other direct City water users). Delivery of water to Santa Clara may be subject to minimum and maximum water delivery levels, which will be negotiated between the City and Santa Clara, provided that Santa Clara's service area and maximum annual usage shall not exceed that set forth in Exhibit M.

(iii) Finally, the City may elect to terminate its water service to Santa Clara. If the City elects to exercise this option, it shall notify Santa Clara of its intention to do so no later than July 1, 1985, and the termination of service shall occur no earlier than July 1, 1987.

(c) In signing this Agreement, neither San Jose nor Santa Clara waives any of its rights to contend, in the event the City does not elect to take it on as a permanent customer in 1987, that it is entitled to that status and to be charged rates identical to those charged other suburban purchasers under this Agreement, pursuant to the Raker Act or any other federal or state law. In signing this Agreement, the City does not waive its right to deny any or all of such contentions.

If, as the result of litigation between San Jose and/or Santa Clara, on the one hand, and the City, on the other, a court of competent jurisdiction enters a final judgment declaring that San Jose and/or Santa Clara are entitled to become permanent water customers of the City and/or compelling the City to provide water to San Jose and/or Santa Clara on a permanent basis, water provided to San Jose and Santa Clara thereafter shall be included within the Supply Assurance.

(d) If the City initially elects to sell water to San Jose and/or Santa Clara on a temporary and interruptible basis pursuant to subsections (a)(ii) and/or (b)(ii), *supra,* it may thereafter elect to take on San Jose and/or Santa Clara as permanent customers, pursuant to subsections (a)(i) and/or (b)(i), *supra,* provided that it so elects on or before June 30, 1988.

Section 9.04. *City of Hayward.*

The City and the City of Hayward ("Hayward") entered into a water supply contract on February 9, 1962 (the 1962 contract) which provides, *inter alia,* that the City will supply Hayward with all water supplemental to sources and supplies of water owned or controlled by Hayward as of that date, in sufficient quantity to supply the total water needs of the service area described on an exhibit to the 1962 contract "on a permanent basis."

The intention of the parties is to continue the 1962 contract in effect, as the individual water supply contract between the City and Hayward. Accordingly, it shall not be necessary for the City and Hayward to enter into a new Individual Contract pursuant to this Article and approval of this Agreement by Hayward shall constitute approval of both this Agreement and an Individual Contract for purposes of Section 2.01. The 1962 contract will continue to describe the service area of Hayward, while rates for water delivered to Hayward during the Term of this Agreement shall be governed by Article IV hereof. The 1962 contract will continue in force after the expiration of the Term of this Agreement.

Section 9.05. *Estero Municipal Improvement District.*

The City and the Estero Municipal Improvement District ("Estero") entered into a water supply contract on August 24, 1961, the term of which continues until August 24, 2011 (the 1961 contract). The 1961 contract provides, *inter alia,* that the City will supply Estero with all water supplemental to sources and supplies of water owned or controlled by Estero as of that date, in sufficient quantity to supply the total water needs of the service area described on an exhibit to the 1961 contract.

The intention of the parties is to continue the 1961 contract in effect, as the Individual Contract between the City and Estero. Accordingly, it shall not be necessary for the City and Estero to enter into a new Individual Contract pursuant to this Article and approval of this Agreement by Estero shall constitute approval of both this Agreement and an Individual Contract for purposes of Section 2.01. The 1961 Contract shall continue to describe the service area of Estero, rates for water delivered to Estero during the Term of this Agreement shall be governed by Article IV hereof, and the 1961 contract will continue in force after the expiration of the Term of this Agreement for the balance of its Term (i.e., until August 24, 2011). The supply guarantee applicable to Estero shall be determined by reference to the 1961 contract, as of the calendar year prior to its expiration (i.e., 2010).

Section 9.06. *Alameda County Water District.*

The City and the Alameda County Water District ("Alameda") entered into a water supply contract on November 30, 1965, the term of which continues until November 30, 1985 (the 1965 contract). The 1965 contract provides, *inter alia,* that the City will supply Alameda with specified quantities of water during its term in accordance with a schedule of deliveries, for use in the service area described in an exhibit to the 1965 contract. The schedule of deliveries specifies that from Fiscal Year 1981/82 until the expiration date of the 1965 contract, the deliveries will range from a

minimum of 5.36 mgd on a monthly basis to a maximum of 16.08 mgd on a daily basis and that the City is not obligated to furnish water at an instantaneous rate of delivery (i.e., during a maximum hour) at more than 120% of the rate of the 16.08 mgd maximum day rate.

The parties intend to continue the 1965 contract for the balance of its term (i.e., until November 30, 1985), during which the minimum monthly and maximum daily and hourly deliveries will continue as provided in the 1965 contract. The parties also intend to determine Alameda's supply guarantee for purposes of Section 7.02 by reference to Alameda's actual water usage during calendar year 1984. (Exhibit K-1, which contains an estimate of that usage, will be automatically amended when the actual usage data for 1984 become available.) The parties further intend, however, to enter into a new water supply contract prior to May 25, 1984 concurrently with their approval of this Agreement, which will serve as the Individual Contract for the balance of the Term of this Agreement. This new contract will contain minimum water delivery levels and may contain maximum water delivery levels, as provided in Section 7.07.

Section 9.07. *Dimond Public Utility District/City of Daly City.*

The City and the City of Daly City ("Daly City") entered into a water supply contract on December 22, 1960, the term of which ended on January 3, 1981. The City and the Dimond Public Utility District ("Dimond") entered into a water supply contract on December 1, 1960, the term of which continues until November 30, 1985 (the 1960 Dimond contract). Dimond subsequently has merged its water distribution system with Daly City. The parties intend to terminate the 1960 Dimond contract concurrently with the execution of this Agreement and the approval of a new Individual Contract with Daly City with a term of 25 years commencing July 1, 1984. In doing so, however, the parties also intend to determine Daly City's supply guarantee for purposes of Section 7.02 by reference to Daly City's water usage during calendar year 1981, as provided for by the 1960 Daly City contract, and by reference to water usage in the former Dimond service area during calendar year 1984, as provided for by the 1960 Dimond contract. The Daly City guarantee for purposes of Section 7.02 shall be the sum of Daly City's calendar year 1981 usage and the calendar year 1984 usage in the former Dimond service area. (Exhibit K-1, which contains actual 1981 Daly City usage and an estimate of 1984 Dimond usage will be automatically amended when the actual usage data for the Dimond service area in 1984 become available.)

Section 9.08. *Coastside County Water District.*

The City and the Coastside County Water District ("Coastside") entered into a water supply contract on January 12, 1971, the term of which continues until January 11, 1991 (the 1971 contract).

The parties intend to terminate the 1971 contract concurrently with the execution of this Agreement and the approval of a new Individual Contract with a term of 25 years commencing July 1, 1984. The new Individual Contract will modify the 1971 contract in certain respects including the following:

(a) The schedule of estimated deliveries during 1985 and 1990 (7.6 mgd and 10.0 mgd, respectively) will be eliminated, and Coastside will receive water from the City pursuant to the terms of Sections 7.01, 7.02 and 7.03 of this Agreement.

(b) Coastside's supply assurance for purposes of Section 7.02 will be determined by reference to its water usage during calendar year 1981, as provided in Section 7.02 and Exhibit K-1 of this Agreement. Water delivered to Coastside will be included within the Supply Assurance contained in Section 7.01.

Section 9.09. *Stanford University.*

The parties recognize that The Board of Trustees of The Leland Stanford Junior University ("Stanford") operates a non-profit university, and purchases water from the City for redistribution to

the academic and related facilities and activities of the university and to residents of Stanford, the majority of whom are either employed by or students of Stanford. Consistent with its prior contract with the City dated August 18, 1960, Stanford agrees that all water furnished by the City shall be used by Stanford only for domestic purposes and those directly connected with the academic and related facilities and activities of Stanford, and no water furnished by the City shall be used in any area now or hereafter leased or otherwise used for commercial or industrial purposes. Stanford further agrees not to use any water from any source whatsoever not in accordance with the foregoing provisions of this Section by substituting therefor water purchased from the City, without obtaining the prior written approval of the General Manager of the SFWD.

Nothing in this Agreement shall preclude the City from selling water to any county, city, town, political subdivision or other public agency for resale to Stanford or to customers within the service area of Stanford.

Notwithstanding anything in Section 7.06 to the contrary, Stanford shall have the right to assign to a public agency having the power of eminent domain all or a portion of the rights of Stanford under this Agreement or the individual contract between it and the City in connection with the acquisition by such public agency of all or a portion of Stanford's water system. In the event of any such assignment of all the rights, privileges, and obligations of Stanford under such contract, Stanford shall be relieved of all further obligations under such contract, provided that the assignee public agency expressly assumes Stanford's obligations thereunder. In the event of such an assignment of a portion of the rights, privileges, and obligations of Stanford under such contract, Stanford shall be relieved of such portion of such obligations so assigned thereunder, provided that the assignee public agency shall expressly assume such obligations so assigned to it.

Nothing in this Agreement shall require or contemplate any delivery of water to Stanford in violation of the Raker Act, which statute imposes certain obligations upon the City as a grantee from the United States in regard to the disposal of water and electricity from the Hetch Hetchy project.

Section 9.10. *City of Brisbane, Guadalupe Valley Municipal Improvement District, Town of Hillsborough.*

The parties acknowledge that the City has heretofore provided certain quantities of water to the City of Brisbane ("Brisbane"), Guadalupe Valley Municipal Improvement District ("Guadalupe") and the Town of Hillsborough ("Hillsborough") at specified rates or without charge pursuant to obligations arising out of agreements between the predecessors of the City and these parties, which agreements are referred to in judicial orders, resolutions of the SFPUC and/or the 1960 contracts between the City and Brisbane, Guadalupe and Hillsborough. The parties intend to continue those arrangements and accordingly agree as follows:

(a) Nothing in this Agreement is intended to alter, amend or modify the terms of Resolution No. 74-0653 of the SFPUC or the indenture of July 18, 1908 between the Guadalupe Development Company and the Spring Valley Water Company.

(b) Nothing in this Agreement is intended to alter, amend or modify the Findings of Fact and Conclusions of Law and Judgment dated May 25, 1961 in that certain action entitled *City and County of San Francisco v. Town of Hillsborough* in the Superior Court of the State of California in and for the County of Marin, No. 23282, as modified by the Satisfaction of Judgment filed October 23, 1961 and the Compromise and Release between Hillsborough and the City dated August 22, 1961. The rights and obligations of the City of Hillsborough under these documents shall continue as therein set forth.

(c) Nothing in this Agreement is intended to affect or prejudice any claims, rights or remedies of Guadalupe or of Crocker Estate Company, a corporation, or of Crocker Land Company, a corporation, or of the City, or of their successors and assigns, respectively, with respect to or

arising out of that certain deed dated May 22, 1884, from Charles Crocker to Spring Valley Water Works, a corporation, recorded on May 24, 1884, in Book 37 of Deeds at page 356, Records of San Mateo County, California, as amended by that certain Deed of Exchange of Easements in Real Property and Agreement for Trade in Connection Therewith, dated July 29, 1954, recorded on August 4, 1954, in Book 2628, at page 298, Official Records of said San Mateo County, or with respect to or arising out of that certain action involving the validity or enforceability of certain provisions of said deed entitled *City and County of San Francisco v. Crocker Estate Company,* in the Superior Court of the State of California in and for the County of Marin, No. 23281.

CITY AND COUNTY OF SAN FRANCISCO

DATED: _____

By _____
Rudolph Nothenberg, General Manager
of Public Utilities

Authorized by Public Utilities Commission

Resolution No. _____

Adopted _____

_____
Romaine A. Boldridge, Secretary

Approved as to form:

GEORGE AGNOST
City Attorney

By _____
McMorris M. Dow, Utilities General Counsel

Approved by Board of Supervisors

Resolution No. _____

Adopted _____

_____
John L. Taylor, Clerk