KEKER & VAN NEST LLP
JOHN KEKER - # 49092
jkeker@kvn.com
DANIEL PURCELL - # 191424
dpurcell@kvn.com
DAN JACKSON - # 216091
djackson@kvn.com
WARREN A. BRAUNIG - # 243884
wbraunig@kvn.com
633 Battery Street
San Francisco, CA 94111-1809
Telephone: 415 391 5400
Facsimile: 415 397 7188

DANIEL S. HENTSCHKE - # 76749
dhentschke@sdcwa.org
General Counsel
SAN DIEGO COUNTY WATER AUTHORITY
4677 Overland Avenue
San Diego, CA 92123-1233
Telephone: (858) 522-6791
Facsimile: (858) 522-6566

Attorneys for Plaintiff
SAN DIEGO COUNTY WATER AUTHORITY

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SUPERIOR COURT OF THE STATE OF CALIFORNIA

IN AND FOR THE COUNTY OF SAN FRANCISCO

SAN DIEGO COUNTY WATER AUTHORITY,

Petitioner and Plaintiff,

v.

METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA; ALL PERSONS INTERESTED IN THE VALIDITY OF THE RATES ADOPTED BY THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA ON APRIL 13, 2010 TO BE EFFECTIVE JANUARY 2011; and DOES 1-10,

Respondents and Defendants.

Case No. CPF-10-510830
Case No. CPF-12-512466

SAN DIEGO'S POST-TRIAL BRIEF FOR PHASE II

Date: June 5, 2015
Time: 2:00 p.m.
Dept.: 304
Judge: Hon. Curtis E.A. Karnow

Date Filed: June 11, 2010
June 8, 2012

Trial Date: March 30, 2015

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I. INTRODUCTION

The Phase II trial was supposed to be about damages. So San Diego proved its damages: $188,295,602, plus interest. But Met went off on a long tangent that had nothing to do with damages, and was also irrelevant to liability, which had already been established in Phase I. Indeed, Met's digression accomplished nothing except to conclusively establish that its affirmative defenses have no merit. Met then failed to introduce any admissible evidence to support its own damages theory, and ultimately conceded that San Diego's damages calculation is correct. The Court, therefore, should award San Diego $188,295,602 in damages, plus interest.

San Diego's damages expert, Dan Denham, testified that he calculated San Diego's damages on the basis of corrected wheeling rates for 2011 to 2014—that is, wheeling rates that Met could have charged in those years if it had not breached the parties' Exchange Agreement by including costs in its Price that, under the Court's Phase I decision, Met had no legal or contractual basis for including. In Phase I, the Court found that Met had no basis for including "in its transportation rates, and hence in its wheeling rate"—and hence in its Price, which is comprised of those transportation rates—"100% of (1) the sums it pays to the California Department of Water Resources' SWP disaggregated by the SWP as for transportation of that purchased water; and (2) the costs for conservation and local water supply development programs recovered through the Water Stewardship Rate." Apr. 24, 2014 Statement of Decision ("SOD") at 65. The Court concluded that "these rates over-collect from wheelers, because at least a significant portion of these costs are attributable to supply, not transportation." *Id.*

Ever since the Court's Phase I decision, Met has hinted that in Phase II it would try to prove some lawful basis for including some ***other*** portion of those costs—less than 100% but greater than zero—in its Exchange Agreement Price. At trial, however, Met failed to introduce any such evidence. On the contrary, Met's damages expert, Christopher Woodcock, who admitted that Met must allocate its costs based on "cost causation" principles, further admitted that the Exchange Agreement "didn't impact the costs of the State Water Project.… didn't impact the costs to Metropolitan," and "did not change or cause any [SWP] costs." Tr. at 1868:20-1869:11, 1933:2-1935:21 (Woodcock). Having thus admitted the absence of any cost-

causation basis for Met to charge any of its SWP costs in the Exchange Agreement Price, Mr. Woodcock did not even attempt to justify including any of the Water Stewardship Rate in the Price. *See id.* at 1910:10-1913:20. And Met's Water Resources Manager, Devendra Upadhyay, admitted that "Met could supply and deliver water to its member agencies without charging for water stewardship," and posed the question to himself, tellingly: "Does the wheeling itself cause Metropolitan to spend more money on demand management?… I don't think so." Tr. at 1418:14-18, 1428:25-1429:7 (Upadhyay). Thus, it is beyond legitimate dispute that it was proper for Mr. Denham to remove all of the SWP costs, and the Water Stewardship Rate in its entirety, from the Price Met charged San Diego from 2011 to 2014.

Indeed, Met's purported rebuttal of Mr. Denham's damages calculation turned out to be nothing more than Mr. Woodcock "putting aside the Court's opinion." Tr. at 1869:16-21 (Woodcock). Otherwise, Mr. Woodcock admitted: "I don't disagree with what [Mr. Denham] did and how he calculated it." Tr. at 1911:11-21 (Woodcock). "The math was proper in what he did with that." *Id.* at 1913:21-1914:2, 1916:7-20. "I don't have any quarrel with the math." *Id.*

What Mr. Woodcock does have a quarrel with is this Court's Phase I opinion. In fact, Mr. Woodcock's alternative damages theory directly contradicts the Court's ruling that it "does [not] matter whether Met delivers a blend of water to wheelers. The blend might be useful"—because it "provides lower salinity water," for example—"but as to wheelers, the benefit is gratuitous, and not required by wheeling agreements." SOD at 53 & n.81 (citation omitted). Despite that ruling, Mr. Woodcock's alternative damages theory was based on his speculation about the possibility of a wheeling rate that would vary according to the blend of SWP water Met decides, in its sole discretion, to provide. Legal, factual, and evidentiary problems with Met's damages theory abound, and are discussed below, but given the Court's instruction that "[w]e are not going to use this phase to revisit the first phase," Tr. at 1880:8-9 (Court), it should be sufficient to note that Met's damages theory contravenes the Court's Phase I decision.

With nothing to say about damages other than to contradict the Court's opinion, Met spent most of its time in Phase II on picayune topics such as the votes of San Diego's Met delegates in years ***other*** than 2010 and 2012. But 2010 and 2012 are the years when Met adopted the 2011-

2014 rates at issue in this case, and it is undisputed and indisputable that San Diego voted against those rates—again, the only ones for which San Diego seeks damages here. Indeed, as the Court knows from Phase I, San Diego not only voted against Met's unlawful 2011-2014 rates, San Diego did everything it possibly could leading up to that vote to get Met to adopt lawful rates—hiring experts and lawyers to explain to Met the governing cost-causation principles and legal standards, and making essentially the same arguments San Diego prevailed on in Phase I. The evidence overwhelmingly disproves Met's contention that despite all of that, San Diego somehow agreed to Met's unlawful rates. Indeed, in Phase I, Met ***admitted*** that, in the negotiations leading to the Exchange Agreement, and in the Exchange Agreement itself, San Diego "***reserved its right to challenge the validity of MWD's rates***" after five years, and "***openly threatened to litigate over MWD's existing rate structure***." Met's Oct. 18, 2013 Pretrial Br. at 14 (emphases added).

Met also spent an inordinate amount of time at trial asking San Diego's witnesses when they first used the word "illegal" to describe Met's rates, as opposed to "not lawful," or "improper," or any number of other variations on the theme. None of that matters in the slightest. San Diego could not and did not consent to Met's unlawful cost misallocations in perpetuity by supposedly failing to use the magic word in some year other than the years actually at issue in this case. On the contrary, Met agreed that there could be no waiver of San Diego's right to challenge Met's rates and seek contract damages "unless it is in writing," and that "no waiver will constitute a continuing waiver unless the writing so specifies." PTX-65 (Exchange Agr.) § 13.9. ***Met admits that no such writing exists***. *See* Tr. at 1337:21-1339:6 (Kightlinger).

Finally, on the issue of San Diego's preferential rights to water under Water Code § 109-135, the Court should hold—as the Court already indicated in denying Met's summary-adjudication motion—that San Diego does not pay Met for the "purchase of water" when San Diego pays Met to convey water San Diego purchases from someone else, such as the Imperial Irrigation District ("IID"). *See id.*; Dec. 4, 2013 Order at 5-7. San Diego's conveyance payments, therefore, should count toward San Diego's preferential rights. *See id.*

For these reasons and others discussed below, the Court should award San Diego $188,295,602 in damages, plus interest. The Court also should issue a declaration that San

Diego's conveyance payments should count toward its preferential rights. And the Court should set a schedule for further briefs and a hearing regarding interest and attorneys' fees.

II. PROCEDURAL HISTORY

In its Phase I opinion, the Court already described the history of this case leading up to that opinion. *See* SOD at 2-4. San Diego will not repeat that history here. But the Court's December 4, 2013 Order denying Met's motion for partial summary adjudication on San Diego's contract and preferential-rights claims is particularly relevant for present purposes because it effectively disposed of arguments that Met, nonetheless, continues to assert.

With respect to San Diego's contract claims, the Court held: "To be sure, San Diego paid its bills under the contract and did not bring a legal challenge to the 2003-2007 rates. But this is not a concession that the rates complied with law, only that San Diego was complying with the five year hiatus agreement." Dec. 4, 2013 Order at 4. "Moreover, the five-year cooling off period in the Exchange Agreement supports the inference that San Diego intended to retain the ability to challenge the rates under applicable law after the end of that period." *Id.* n.9.

And, with respect to preferential rights, the Court rejected Met's attempt at a syllogism. Met argued, and continues to argue, along the following lines: (a) the Price San Diego pays under the Exchange Agreement consists of the System Access Rate, System Power Rate, and Water Stewardship Rate; (b) those rates are also included, along with the Supply Rate, in Met's charges for purchase of water; therefore (c) the Price must be for purchase of water. As the Court held: "The flaws in the reasoning include: (a) the components are not the same, for Price includes only some of the four items; (b) critically, the one item it does not include is the cost of water, and concomitantly (c) San Diego has already paid ***someone else*** (a third party such as Imperial) for the 'purchase of water.'" Dec. 4, 2013 Order at 7 (emphasis in original).

The Court issued its Phase I opinion on April 24, 2014:

> Met's contract with the state makes clear that Met does not own or operate the SWP transportation facilities. Previously, Met allocated SWP costs to supply, and ***none to transportation*** (including the SWP costs that DWR bills as its own transportation costs). ***No reasonable basis appears in the record as to why this has changed***.… ***Nor does it matter whether Met delivers a blend of water to wheelers. The blend might be useful but, as to wheelers, the benefit is gratuitous, and not required by wheeling agreements***.…

> [T]he Water Stewardship Rate recovers the costs of 'demand management programs,' and … the ***primary*** benefit is not for transportation, but for supply.… While wheelers would benefit as a general matter by reason of increased capacity in that they might be able to wheel more water, those who in fact are permitted to wheel do so in a system built out to move non-wheeled water, that is, water that Met sells to its member agencies. Thus the costs and avoided costs attributable to the demand management programs relate to the transportation needs to provide purchased water. This too suggests that the cost of wheeling, while properly a function of system-wide costs associated with transportation as such, ***should not be a function of system-wide avoided costs of transporting purchased water***.…
>
> Indeed, the record confirms that ***these rates over-collect from wheelers***, because at least a significant portion of these costs are attributable to supply, not transportation. These rates – the System Access Rate, System Power Rate, Water Stewardship Rate, and Met's wheeling rate – therefore violate Proposition 26 (2013-14 rates only), the Wheeling statute, Govt. Code § 54999.7(a), and the common law. The Court invalidates each rate for both the 2011-2012 and 2013-2014 rate cycles.

SOD at 53, 58-61, 65 (emphases added) (citations and footnotes omitted).

San Diego then sought to recover damages based on Section 12.4(c) of the Exchange Agreement, which provides that, in the event of a dispute over the Price, Met must set aside the "disputed amount" and pay it to San Diego "forthwith" if San Diego prevails. *See* PTX-65 § 12.4(c). San Diego argued, among other things, that paying this "disputed amount" was an alternative way for Met to perform its obligations under the contract. The Court, however, agreed with Met that paying the disputed amount is not an alternative means of performance because "***it is manifest that Met is required to perform the contract by setting a lawful price***." Nov. 4, 2014 Order re Damages at 10 (emphasis added).

Accordingly, the parties proceeded to the Phase II trial on contract damages. In response to Met's repeated assertions that damages can only be determined by setting alternative lawful rates that the Court lacks jurisdiction to decide, the Court cautioned Met that it "should not propose a theory or procedure on contract damages which it simultaneously contends [the Court] must not undertake (as a result of arguments on jurisdiction, power, comity, or other grounds)." Nov. 4, 2014 CMC Order at 1-2; *see also* Dec. 4, 2014 Order at 1-2. "Even if damages are difficult to determine, a trial court nevertheless should attempt to do so if there is liability." Nov. 4, 2014 CMC Order at 2 n.2 (citing *Meister v. Mensinger*, 230 Cal. App. 4th 381 (2014)).

The Court held the Phase II trial over the course of six days between March 30, 2015 and April 29, 2015, hearing evidence on San Diego's contract damages, on preferential rights, and on

Met's affirmative defenses of waiver, consent, estoppel, mistake of law, illegality of contract, offset, and unjust enrichment.[1]

III. FACTUAL BACKGROUND

A. The background and relevant terms of the 1998 Exchange Agreement

The Colorado River "is the most legislated, most debated, and most litigated river in the entire world." MARC REISNER, CADILLAC DESERT 120 (2d ed. 1993). Indeed, this case has its origins in "one of the longest-running lawsuits in the annals of the Court," *id.* at 260-61—*Arizona v. California*, 373 U.S. 546 (1963), which held that California must restrict its use of Colorado River water to 4.4 million acre-feet per year (MAFY).[2] That allotment is distributed according to a priority system whereby Colorado River water goes to the second priority only after the first priority has taken its full entitlement, and so on up to the fourth priority—the limit of California's 4.4 MAFY allotment—which can only be exceeded "in times of surplus on the Colorado River." Tr. at 187:10-18 (Cushman); *see also* PTX-60 Attach. 1 at 1; Tr. at 1277:14-1281:1 (Kightlinger). Met's basic entitlement to Colorado River water is fourth in priority, and is "only about 550,000 acre-feet, leaving the Colorado River Aqueduct, which has an approximate capacity of more than 1.2 million acre-feet per year, ***over half empty***." *QSA*, 201 Cal. App. 4th at 785 (emphasis added) (quotation marks and brackets omitted); *accord* Tr. at 1277:14-1281:1 (Kightlinger). IID, on the other hand, is third in priority, which means that in times of shortage, IID "is entitled to divert its

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[1] As San Diego pointed out before trial, Met previously indicated that it might assert a "'timeliness'" defense, which "'can be resolved by briefing,'" but Met waived that defense by failing to file any motion or brief asserting it. San Diego's Mar. 23, 2015 Pretrial Br. at 19 n.6 (citation omitted). Met never responded and, indeed, never even mentioned its purported "timeliness" defense at trial. That affirmative defense is certainly waived now.

[2] Met directed California's doomed legal strategy in *Arizona*, which "wasn't so much a legal argument as a game of chicken with the Supreme Court. In effect, the Met was daring the Court to take away water for three million people just as they were coming to depend on it." CADILLAC DESERT at 349. Because Met was arguing in *Arizona* that California needed every drop it was taking from the Colorado River, Met originally fought against the proposed SWP "hammer and tongs, arguing against it on every conceivable ground: cost, need, feasibility, practicality, even morality." *Id.* at 349-50. Met ultimately reversed its position, however, and now charges its SWP costs to the transportation of Colorado River water from IID, even though transporting that water does not cause any SWP costs at all, and is actually the solution—for all of California—to the problems that resulted from Met's defeat in *Arizona*. *See In re Quantification Settlement Agreement* ("*QSA*") *Cases*, 201 Cal. App. 4th 758, 785-89 (2011). "In California, when the issue is water, the ironies seem to string out in seamless succession." CADILLAC DESERT at 373.

full right to water before Metropolitan can divert any water at all." *Cnty. of Imperial v. Superior Court*, 152 Cal. App. 4th 13, 19 (2007).

Long before San Diego acquired water from IID, it was well understood that if IID could sell conserved water to Met or one of Met's member agencies, that would help solve the interrelated problems of California's reduced allotment of Colorado River water, the half-empty Colorado River Aqueduct, and the need to provide "conservation incentives" for farmers in the Imperial Valley. Dec. 23, 2013 Req. for Jud. Not., Ex. 1 ("Wheeling Leg. Hist.") at LH362; *see also* Tr. at 774:2-775:5 (granting request for judicial notice). Indeed, these were the fundamental reasons for legislation in the 1980s—specifically including the Wheeling Statutes—designed to foster water markets. *See* Wheeling Leg. Hist. at LH93, 151, 362, 372, 374, 380-81. Nevertheless, by the mid-1990s—three decades after the *Arizona* decision, a decade after the Legislature had enacted the Wheeling Statutes and related water-marketing legislation, and even after five years of drought, from 1987 to 1992, had resulted in massive water shortages for Met and its member agencies—Met had only secured about 105,000 acre-feet per year of IID water (and even that was subject to claims by Coachella Valley Water District under the priority system). *See id.*; PTX-15 at I-1; PTX-60 Attach. 1 at 1-2; Tr. at 173:7-24 (Cushman), 1271:7-1272:10 (Kightlinger).

The 1987-1992 drought was particularly hard on San Diego, which was almost completely dependent on Met water, and suffered water shortages of 31% for more than a year. Tr. at 173:7-24 (Cushman). Painfully aware of the need for more reliable sources of water supply—and also aware that IID could conserve more water through fallowing and other extraordinary conservation measures, and that there would be ample capacity available in the Colorado River Aqueduct once California was actually limited to its 4.4-MAFY allotment—San Diego began negotiating its own agreement with IID. *See id.*; Tr. at 1246:13-16 (Slater), 1277:14-1281:1 (Kightlinger); *QSA*, 201 Cal. App. 4th at 785, 788. As the Court knows from Phase I, Met's response to those negotiations was to adopt, in January 1997, a wheeling rate that Met had begun designing in 1995 with the explicit goal of discouraging wheeling in general, and the IID-San Diego transfer in particular. *See, e.g.*, AR2010-1234-35, 1245, 1248-49 (RMI); AR2010-2446-51 (Resolution

8520); SOD at 55-58.[3] From that time to the present, San Diego has repeatedly complained to Met that its "wheeling rates are contrary to the law, bad public policy, and an obstacle to critically needed water transfers to the Southern California coastal plain." AR2010-2942.[4]

In October 1997—while Met's unsuccessful effort to validate its 1997 wheeling rate was winding its way through the courts—the Legislature passed an emergency bill directing the DWR Director, David Kennedy, to help Met and San Diego negotiate a fair wheeling rate, and if they could not agree to one, to "issue a formal recommendation." 1997 Cal. Legis. Serv. Ch. 874 (S.B. 1082). "The director, in issuing a recommendation regarding appropriate terms and conditions of the transfer, shall make those determinations prescribed by Section 1812." *Id.*; *see also* Water Code § 1812 (providing for determinations of "unused capacity" and "terms and conditions, including operation and maintenance requirements and scheduling, quality requirements, term or use, priorities, and fair compensation"). Director Kennedy was "extremely well-regarded" by everyone involved, including the Governor, the Legislature, San Diego, and Met. Tr. at 1170:20-1174:24 (Slater). The Legislature took the unusual step of specifically empowering Director Kennedy to determine fair compensation for Met to wheel the conserved IID water to San Diego because it "is of vital state interest that every effort be made to ensure that the Colorado River Aqueduct continues to operate at its full capacity at fair and reasonable terms in order to minimize statewide disruptions from diminishing Colorado River supplies." S.B. 1082.

In December 1997, Director Kennedy participated in negotiations at which representatives from Met and San Diego presented their respective proposals. *See* PTX-26. San Diego urged that the parties agree to a wheeling rate for a term corresponding to the term of the proposed IID-

[3] Met also waged a no-holds-barred campaign against anyone, including the Governor and members of the Legislature, who supported the IID-San Diego transfer. After Met's activities were exposed, the Legislature passed a special law requiring Met to "establish and operate an Office of Ethics." Water Code § 109-126.7; Cal. B. An. Apr. 7, 1999 (S.B. 60).

[4] *See also*, *e.g.*, Tr. at 218:8-223:12, 259:14-260:19, 990:5-1019:12, 1097:21-1099:15 (Cushman), 712:4-734:25 (Skillman); 1189:14-1196:6, 1201:4-21, 1232:10-1233-19 (Slater), 1365:9-1366:2 (Kightlinger), 1432:1-24 (Upadhyay), 1519:24-1532:18, 1554:7-1562:22, 1563:10-1567:19, 1596:9-1597:17, 1616:19-1619:21, 1623:4-25, 1645:20-1648:13 (Stapleton); PTX-392 (Thomas PMK Dep.) at 58:23-61:25; 121:10-127:5, 133:6-136:10, 143:4-11; AR2010-11203-214; AR2010-11343-92; AR-2010-11564-574; AR2012-16154-16241; AR2012-16215-216; AR2012-16995-17013; AR2012-17098-126; PTX-28 at 118-20; PTX-56; PTX-80-81; PTX-177; PTX-189; PTX-225; PTX-234; PTX-398; DTX-342; DTX-837; DTX-859; DTX-909.

San Diego transfer agreement—45 years, renewable for another 30 years. *See id.* at MWD2010-00264778; PTX-28 art. 4. San Diego proposed that the wheeling rate should compensate Met for its actual costs, but also should give San Diego credit for the region-wide benefits of the Transfer Agreement. As San Diego noted, Met had estimated those regional benefits at $65/AF for all of Met's member agencies, on all Met water, because without the transfer, Met would have to spend more on water supplies "in order to maintain a full Colorado River Aqueduct." PTX-25;[5] *see* PTX-26 at MWD2010-00264779.

Met's counterproposal acknowledged the "significant regional benefits" of the transfer, and proposed a corresponding "discount of more than 50%" off of Met's wheeling rate. PTX-26 at MWD2010-00264786-91. It is important to note, however, that Met's "discount" terminology was, and still is, misleading. First, the costs that Met was supposedly "discounting" are the same ones this Court has now held Met never had any right to include in the first place. *See* SOD at 37-39, 52-61, 65. Second, under the Wheeling Statutes, San Diego is entitled to "reasonable credit for any offsetting benefits for the use of the conveyance system." Water Code § 1811(c). In any event, Met proposed to wheel the transfer water, on an "as available" basis, for $70/AF plus power costs. PTX-26 at MWD2010-00264786. If the aqueduct happened to be full due to a water surplus—although the essential motivation for everyone concerned was the far more likely event of water shortages—San Diego would either store the conserved IID water itself, or pay Met an even higher rate of $120/AF plus power for Met to store the water and then deliver it when space became available. *See id.*

Internally, however, Met's estimates of its actual costs for wheeling were much lower. For example, in July 1996, Brian Thomas (who later became Met's CFO), estimated that a wheeling rate limited to "recovering only the additional costs incurred with providing that service"—which is, incidentally, the type of wheeling rate DWR charges Met, *see* AR2010-1 at 153 § 55—would amount to "about $10/AF plus energy costs." AR2012-17126_103 at 109. Mr.

[5] A handwritten note on this analysis by Met's Shane Chapman asks: "How is this being used? Let's not put ourselves in a position where SDCWA can say, 'See the SDCWA/IID Transfer is worth $1.41/m to $2.82/m for Southern Californians.'" PTX-25. Apparently the cat got out of the bag between July and December 1997. *See id.*; PTX-26 at MWD2010-00264779.

Thomas did not specify an amount for Met's "energy costs," *id.*, but Director Kennedy assumed that Met could "provide power @ $30/acre-foot," PTX-481 at 3, and more recently, in 2010, Met's Jon Lambeck calculated power costs on the Colorado River Aqueduct to be "approximately $50/AF." PTX-479; Tr. at 1788:1-1789:12.[6] Taking those two estimates of power costs as bookends, the cost-causation-based wheeling rate Mr. Thomas suggested internally was between $40/AF to $60/AF, whereas in the negotiations, Met proposed to charge a wheeling rate between $100/AF and $120/AF without storage, or $150/AF to $170/AF with storage.

On January 5, 1998, Director Kennedy recommended a wheeling rate of ***$80/AF***, including power, which was a "compromise between various rates advocated by MWD and SD over the course of the discussions," and "takes into account Metropolitan's fixed system costs and the regional benefits provided by San Diego bringing conserved IID water to the region." PTX-481 at MWD2010-00264720 n.4. Director Kennedy found that a reasonable credit to San Diego for the offsetting regional benefits of the transfer would be $220/AF—a compromise between the $250/AF San Diego would initially be paying IID to conserve the water and the lower $208/AF price Met speculated it would have negotiated with IID. *See id.* n.3. Director Kennedy's proposal was specific to the IID-San Diego transfer "because that is the specific problem before us," but was consistent with "a more generic analysis" that would apply to "Metropolitan and any of its member agencies." *Id.* at MWD2010-00264717. Director Kennedy also noted that, to the extent there might sometimes be surplus Colorado River water, leaving insufficient capacity for the conserved IID water, Met should pay to store that water because Met would be "receiving the

[6] At trial, Mr. Lambeck attempted to testify about Met's purportedly higher power costs for transporting water under the Exchange Agreement, but the Court rightly sustained San Diego's objections to much of Mr. Lambeck's testimony, as well as his documents. *See, e.g.*, Tr. at 1724:9-20 (Court). The remainder of Mr. Lambeck's testimony proves that Met does not actually incur the purportedly higher power costs Mr. Lambeck tried, but failed, to introduce into evidence. On the contrary, Mr. Lambeck admitted that Met's actual cost of power on the Colorado River Aqueduct—for both Exchange water and Met water—is the much lower "melded" Colorado River power rate. *See* Tr. at 1715:14-1718:12, 1746:15-1747:10, 1765:24-1768:5, 1777:6-1779:11, 1783:6-1790:12 (Lambeck). Because of this and Met's other failures to come to terms with the relevant facts, evidence and law (as discussed further below), Met's damages theory fell apart completely at trial, as Met conceded. *See, e.g.*, Tr. at 1835:6-8 ("Mr. Quinn: Your Honor, obviously, this is at the heart of our alternative damages case and obviously we have some issues here.…"); *see also* § IV.C, *infra*.

benefits" of it and, as "a practical matter," Met "would undertake these storage arrangements if it did the IID deal." *Id.* at MWD2010-00264718. In any event, as Scott Slater, San Diego's lead contract negotiator, testified, the "projections at that time, which proved to be true," were that "the aqueduct would rarely, if ever, be full again." Tr. at 1162:16-1164:2, 1246:13-15 (Slater).

Because everyone trusted Director Kennedy, his proposed $80/AF wheeling rate "had influence on public sentiment about what was an appropriate wheeling charge and set an environment for negotiation of the wheeling rate." Tr. at 1171:13-1174:24 (Slater). Accordingly, on January 13, 1998, Met's Board directed its negotiators to proceed "within the framework proposed by Director David Kennedy." AR2010-2972 at 2977. On April 29, 1998, San Diego and IID executed their Transfer Agreement based, in part, on the assumption that San Diego and Met would be able to agree to a wheeling rate along the lines Director Kennedy had proposed. *See* PTX-28 § 7.1(e). And on November 10, 1998, San Diego and Met executed the 1998 Exchange Agreement. PTX-31.

The 1998 Exchange Agreement mooted Met's purported concern about the possible availability of surplus water on the Colorado River—which Met had been able to obtain in the past at no cost, but which by this time was little more than a fond memory given the pressure for California to limit itself to 4.4 MAFY—by providing that San Diego would make a certain amount of conserved IID water available to Met every year, and Met would make that quantity and quality of water available to San Diego in monthly installments. PTX-31 art. III. The price was based on Director Kennedy's recommended $80/AF wheeling rate.[7] It would start at $90/AF and then increase by 1.55% per year for 20 years, after which it would reset to Director Kennedy's $80/AF wheeling rate, and then increase by 1.44% for 10 years. PTX-31 § 5.2. After 20 years, Met could seek adjustments "necessary to reflect reasonable changes in Metropolitan's net costs," but expressly "excluding any costs of the State Water Project." *Id.* § 5.4.

[7] Met argued in Phase I, and still argues in Phase II, that the price terms in this and the operative Exchange Agreement should not be evaluated as wheeling rates because the contracts are not called wheeling contracts. That is a *non sequitur*, as the Court succinctly pointed out in Phase I: "I don't think the thought is that this agreement is a wheeling agreement. I think the thought is that the rates that they're paying are wheeling charges." Tr. at 233:21-24 (Court). That is exactly what the evidence shows. *See, e.g.*, Tr. at 1646:9-24 (Stapleton).

Met's obligations under the 1998 Exchange Agreement were subject to several conditions precedent, including "legal authorization, appropriation, and a legally binding commitment of the State of California" to provide $235 million for lining the All-American and Coachella Canals. *Id.* § 8.1(d). Those conditions precedent posed a serious risk to San Diego. If any of them was not satisfied—for example if the State ultimately did not provide the $235 million for the canal-lining project—Met could simply back out of the deal, leaving San Diego with no agreement for wheeling its conserved IID water. Tr. at 1167:3-1170:5 (Slater), 1525:17-1526:24 (Stapleton).

The 1998 Exchange Agreement also posed additional risks for San Diego due to the discrepancy between its 30-year term and the 45- to 75-year term of the Transfer Agreement. That discrepancy was no accident. San Diego had sought a 45-year term, but Met would not agree to anything beyond 30 years. Indeed, the 1998 Exchange Agreement explicitly provided that San Diego would "not have a right to extension or renewal of such thirty-year term," even though "the Transfer Agreement calls for a 45-year term." PTX-31 § 10.6.[8] By the last 15 years of the Transfer Agreement, the transfers would have ramped up to their maximum of 200,000 acre-feet per year, meaning that, for those last 15 years, San Diego would be paying for the conservation of 3 million acre-feet of IID water, with no commitment from Met to wheel it at any price but, instead, the risk that Met would try to extract the costs Met believed—wrongly, as the Court found in Phase I—Director Kennedy should have included in his recommended wheeling rate. *See* Tr. at 1009:7-1010:1, 1068:7-17 (Cushman), 1164:3-1166:3 (Slater), 1525:17-1526:24 (Stapleton), 1288:8-1289:11 (Kightlinger); PTX-507.

B. The negotiation and relevant terms of the operative Exchange Agreement

San Diego's concerns about the mismatch between the respective terms of the Transfer Agreement and the 1998 Exchange Agreement were largely dormant from 1998 to 2003 because it was unclear during that time whether either agreement would ever reach even the first year. Tr. at 1006:4-11 (Cushman), 1166:8-12 (Slater). Despite the Legislature's 1997 findings about the

[8] Reading Section 10.6 of the 1998 agreement, one can almost hear ominous background music, or perhaps James Brown's The Payback, which is surprisingly (albeit unintentionally) apt: "I can do wheeling … that's a fact … [but] get ready … for the big payback." *Id.*

"urgency" of California's need for the IID-San Diego water transfer, S.B. 1082, and despite Met's own description of the Transfer Agreement as "the linchpin of the California 4.4 Plan," and a "key part of the solution to California's statewide water shortage problem," PTX-30, no water had been transferred because—among other issues ultimately addressed in the set of agreements known as the QSA—Met was fighting the Transfer Agreement in court. *See Imperial*, 152 Cal. App. 4th at 20-21. Met argued that IID had nothing to transfer because "any water unused by [IID] is available to [Met] under the priority system." *Id.* at 20. It later became clear, however, that this was simply extortion, as Met began to hint that its "objections could be resolved as part of a broader resolution of Colorado River issues," and then dropped those objections in return for an agreement "to reduce the water transfer to San Diego from 300,000 afy to 200,000 afy, and to make the 100,000 afy difference available for acquisition by Metropolitan and Coachella." *Id.* at 21-22; *see also QSA*, 201 Cal. App. 4th at 788.

Another reason why no conserved IID water had yet been transferred to San Diego was Met's position that the canal-lining condition precedent in the 1998 Exchange Agreement had not been satisfied, and might never be satisfied. As Mr. Slater explained: "It was the summer of 2003, and the State was in a pretty historic budget crisis. And there had been runs on various funds that had been set aside." Tr. at 1167:3-1169:7 (Slater). Ron Gastelum, Met's General Manager and CEO at the time, had made clear that Met would contend that the condition precedent had not been satisfied because Met might never receive the $235 million from the State to line the canals. Tr. at 1169:7-25 (Slater), 1525:17-1526:24 (Stapleton).

San Diego's goals in negotiating the operative Exchange Agreement were to reduce its risks of not having an agreement or price terms in place for transporting the conserved IID water for the last 15 years of the Transfer Agreement, and to eliminate any further delay due to Met's contention that the canal-lining condition precedent had not been satisfied. *See id.* Met's goal was to get San Diego to pay the wheeling rate Met had been fighting for, and San Diego had been fighting against, since before Met first adopted it in 1997. The compromise the parties agreed to was, in essence, that each party would bear the risk that its own long-held positions might prove to be unsuccessful, if and when, after a five-year peace treaty (during which the parties would

continue to try to work things out), they went back to court over Met's wheeling rates, as they had done in the late 1990s. *See* Tr. at 995:15-996:9, 1002:17-1005:5 (Cushman), 1176:6-1201:21 (Slater), 1519:24-1532:18, 1554:7-1562:22, 1563:10-1567:19 (Stapleton).

As Maureen Stapleton, San Diego's General Manager, and Jeff Kightlinger, Met's General Manager and CEO, both testified, San Diego believed that a wheeling rate along the lines of what Director Kennedy had found to be fair—"somewhere around $80, $90 an acre-foot"—was, indeed, fair. Tr. at 1289:10-11 (Kightlinger); *see also* Tr. at 1472:15-21, 1600:1-8 (Stapleton). Met, on the other hand, "believed that the true cost of conveying the water to San Diego was somewhere around $250 an acre-foot," which included the disputed SWP costs and Water Stewardship Rate. Tr. at 1288:13-1289:11 (Kightlinger). San Diego decided that agreeing to pay Met's wheeling rate for five years "was worth the risk" if San Diego "could put boundaries on [its] exposure to Met's wheeling rate and had the opportunity to either negotiate something [the parties] could both live with" or, "[a]fter five years, if we were unsuccessful reaching an agreement on what would be considered the lawful rate, the Water Authority had the ability to contest the wheeling rate that Met had established in either an administrative or judicial manner." Tr. at 1525:25-1530:13 (Stapleton). Accordingly, San Diego agreed to "enter into a contract where there is a disagreement" about the law—in other words, agreed to disagree—while reserving the "right to challenge after five years." Tr. at 1596:9-1597:17 (Stapleton).

From San Diego's perspective, five years was a reasonable length of time to agree to pay Met's wheeling rates because, for those first five years, the total amount of water to convey was only 150,000 acre-feet, as opposed to the 3 million acre-feet San Diego would need Met to convey in the last 15 years of the Transfer Agreement, after the 1998 Exchange Agreement would have expired. Tr. at 1009:7-1010:1, 1068:7-17 (Cushman), 1164:3-1166:3 (Slater), 1525:17-1526:24 (Stapleton). San Diego also knew that it would need to join forces with Met to defend the QSA. Tr. at 1196:7-1197:23 (Slater). San Diego was hoping to finalize negotiations involving "Seven states, two presidents, two governors and couple of secretaries of interior, special intervention litigation," and a score of federal and state agencies and Native American

tribes.[9] *Id.* at 1196:7-16 (Slater). Met, on the other hand, had been trying to sabotage or hijack those negotiations the entire time. *See, e.g.*, *Imperial*, 152 Cal. App. 4th at 20-21; *QSA*, 201 Cal. App. 4th at 788; S.B. 60. But if San Diego could get the deal done despite Met's intransigence, it would be time for "circling the wagons" to "protect the agreements during the five-year period against people who [were] going to be attacking" them, including environmental groups and farming interests in Imperial County. Tr. at 1196:7-1197:23 (Slater).

Accordingly, the parties negotiated what, from the beginning, they called a "Peace Treaty." PTX-58 ¶ 8; PTX-392 (Thomas PMK Dep.) at 127:12-130:14. The initial draft specified that both parties would "agree to not lobby or support any legislative change to wheeling laws for term of agreement." PTX-58 ¶ 8. This no-lobbying provision was important to the parties because, for example, Met had sought in 1998 to amend the Wheeling Statutes to explicitly codify its own view—contrary to the subsequent decision in *San Luis Coastal Unified Sch. Dist. v. City of Morro Bay*, 81 Cal. App. 4th 1044, 1050 (2000)—that the Wheeling Statutes' prohibition against "injuring any legal user of water" includes "shifting costs." AR2010-3093 at 3095. And Met was still smarting over S.B. 1082, pursuant to which Director Kennedy had recommended his $80/AF wheeling rate. *See* S.B. 1082; PTX-481; Tr. at 1238:13-21 (Slater).

The Peace Treaty also provided that San Diego would agree not to bring judicial or administrative challenges to Met's established wheeling rates for five years; and that Met's wheeling rates would be non-discriminatory and apply equally to all member agencies, an important protection for San Diego. PTX-58 ¶ 8. Met had originally proposed that San Diego be precluded from challenging Met's rates, other than on procedural grounds, for the entire 45-year term of the agreement. Failing that, Met proposed that any substantive challenges be limited to the law in existence at the time of the Exchange Agreement's execution. *See* Tr. at 1176:16-1196:6 (Slater); DTX-811; PTX-392 (Thomas PMK Dep.) at 126:6-127:5. Unwilling to agree to

[9] The tribes' tribulations, by the way, show that Met was not the only party taking absurd positions in the *Arizona* litigation. *Cf.* n.2, *supra*. Arizona argued that the tribes were getting "too much" water. Justice Black's response is classic: "It can be said without overstatement that when the Indians were put on these reservations they were not considered to be located in the most desirable area of the Nation." *Arizona*, 373 U.S. at 598.

those terms, San Diego negotiated for terms that allowed it to sue after five years, based on substantive claims, not just procedural ones, and not limited to the law at the time of execution, but based on the law as it evolved. *See id.*; Tr. at 1097:5-20 (Cushman). Both parties also agreed that there could be no waiver of any right or remedy—including the right to sue for damages—except in writing, and even then, no continuing waiver unless that, too, was in writing. *See* Tr. at 1198:15-1201:21 (Slater).

Further, "given Metropolitan's insecurity over funding and other issues related to implementing the canal lining," and to eliminate Met's condition precedent and finally get the conserved IID water, as well as the canal-lining water, flowing to San Diego, San Diego "agreed to flip the obligation and assume the role of implementing the canal lining project under the theory that if Met did not believe this was capable of being implemented or that there were limitations, then San Diego would take that risk." Tr. at 1170:1-19 (Slater). That was done in the Allocation Agreement. As San Diego's Assistant General Manager, Dennis Cushman, testified (contrary to Met's suggestions) the Allocation Agreement was not some sort of sinecure. "Nobody wrote the Water Authority a check for $235 million at the time. We got the Allocation Agreement and got the canal lining and with that came considerable risk in carrying out the project, risks that many people at the time understood would face whichever party constructed the All-American Canal." Tr. at 1068:18-1069:4 (Cushman). Those included inevitable environmental challenges and litigation, and the financial and engineering risks of building "one of the largest canals in the world … through sand dunes" without knowing whether the State would actually come through with the money and, if it did, whether it would be enough. Tr. at 1068:18-1069:18 (Cushman). After all, the history of water in the West is a cautionary tale of massive projects going far over budget, only to produce far less water, and far more litigation, than anticipated. *See generally* CADILLAC DESERT.

In any event (again, contrary to Met's suggestions) this case is not about the Allocation Agreement, but the Exchange Agreement—in particular, Section 5.2 of the Exchange Agreement:

> The Price. The Price on the date of Execution of this Agreement shall be Two Hundred Fifty Three Dollars ($253.00). Thereafter, ***the Price shall be equal to the charge or charges set by Metropolitan's Board of Directors pursuant to***

> ***applicable law and regulation and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies***. For the term of this Agreement, neither SDCWA nor Metropolitan shall seek or support in any legislative, administrative or judicial forum, any change in the form, substance or interpretation of any applicable law or regulation (including the Administrative Code) in effect on the date of this Agreement and pertaining to the charge or charges set by Metropolitan's Board of Directors and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies; provided, however, that Metropolitan may at any time amend the Administrative Code in accordance with Paragraph 13.12, and the Administrative Code as thereby amended shall be included within the foregoing restriction; and, provided, further, that (a) ***after the conclusion of the first five (5) Years, nothing herein shall preclude SDCWA from contesting in an administrative or judicial forum whether such charge or charges have been set in accordance with applicable law and regulation***; and (b) SDCWA and Metropolitan may agree in writing at any time to exempt any specified matter from the foregoing limitation.

PTX-65 § 5.2 (emphases added); *see also id.* § 13.6 (integration clause).

As Mr. Thomas candidly admitted at his deposition as Met's person most knowledgeable about the Exchange Agreement, "***Section 5.2 allows the Water Authority to do what it has done in this case***." PTX-392 at 122:21-123:1 (emphasis added). Mr. Thomas agreed that Section 5.2 means "[w]hat it says: That after the fifth year, San Diego could contest, in a judicial forum or administrative forum, whether Met's rates and charges are consistent with the applicable laws and regulations." *Id.* at 121:21-122:4. Given that the five years have now passed, the provision that applies "[f]or the term of this Agreement" is effectively limited to "legislative" challenges because San Diego is expressly allowed, after five years, to bring "administrative or judicial" challenges. *See id.* at 130:3-14; PTX-65 § 5.2; DTX-811.[10] Likewise, Section 11.1, which also references the five-year peace treaty on "Price Disputes," PTX-65 § 11.1, means that "after five years, [San Diego] could avail themselves of legal remedies." PTX-392 (Thomas PMK Dep.) at 125:24-25; *see also id.* at 58:23-61:25; 121:10-127:5, 133:6-136:10, 143:4-11.

The Price is limited to charges set "pursuant to applicable law and regulation"—*i.e.*, a "lawful wheeling rate," as the parties often phrased it. *See, e.g.*, Tr. at 1004:9-11 (Cushman), 1184:3-1189:2 (Slater), 1526:15-1531:13 (Stapleton); DTX-841 at 3; PTX-56 at MWD2010-

[10] Similarly, the earlier provision that neither San Diego nor Met may seek to change Met's Administrative Code is effectively limited to San Diego by the later clause specifying that Met may change its Administrative Code after all. *See* PTX-65 § 5.2. The structure of Section 5.2, in essence, is "everything is forbidden, except what's allowed." And San Diego was expressly allowed to sue Met over its rates after five years. *Id.*; *see also id.* § 11.1.

00446361-62; PTX-57. Further, the Price must be "generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2. San Diego had always demanded that Met's rates must "be non-discriminatory so that the rates would apply equally to all member agencies." PTX-58 ¶ 8; *see also* Tr. at 1184:3-1185:21 (Slater), 1646:25-1647:12 (Stapleton).[11] Thus, after five years, San Diego was allowed to sue for the recovery of any charges that Met did not set "pursuant to applicable law and regulation and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2; *see also id.* §§ 11.1, 12.3, 12.5, 13.9. The contract precludes, for example, a Price that is unique to San Diego because San Diego received money from the State to line the canals; or a Price that is unique to San Diego because of the ever-changing blend of water that is "determined by Metropolitan" in its "sole discretion." *Id.* §§ 1.1(m), 3.2(e), 3.6. Met may only charge San Diego a lawful ***and*** generally-applicable wheeling rate. *See id.* § 5.2.

Met knew exactly what San Diego meant by a "lawful wheeling rate." *See* PTX-398. As Mr. Thomas told Mr. Kightlinger, "It is clear where SDCWA is headed when they write that the 'lawful wheeling rate [is] generally equivalent to the continuation of the exchange rate identified in the [1998] Exchange Agreement.'" *Id.* (ellipses omitted) (quoting PTX-56 at MWD2010-00446361). "This implies they believe that any rate different than the favorable rate they have received is not lawful and they are already arguing their case in their proposal." PTX-398. As Mr. Kightlinger testified, "San Diego's view" was that a lawful wheeling rate would be "somewhere around $80, $90 an acre foot." Tr. at 1289:6-11 (Kightlinger). In other words—indeed, in Mr. Thomas's own words to Mr. Kightlinger—Met knew that San Diego would maintain that Met's wheeling rate "***is not lawful***." PTX-398 (emphasis added).

Met, along with everyone else with any interest in the QSA, also knew that San Diego had reserved its right to sue after five years over the wheeling rate that, again, San Diego had always

[11] Note, however, that the power component of the wheeling rate in Met's Administrative Code is the wheeling party's "own cost for power" or Met's "actual cost," whereas Met chose to charge San Diego the System Power Rate in the Exchange Agreement Price, for the convenience of Met's own "billing purposes." Met Admin. Code § 4405(b) (DTX-1149A); PTX-78; *see also* PTX-392 (Thomas PMK Dep.) at 114:2-115:8; Tr. at 1647:13-16 (Stapleton).

contended "is not lawful." *Id.* This is clear not only from the Exchange Agreement itself and all of the contemporaneous correspondence, but also from the 2003 Amendment to the Transfer Agreement, which is expressly referenced in the Exchange Agreement, and was executed at the same time at "a signing event at Metropolitan in [the] boardroom where all the parties came in to Los Angeles, and … signed all 30-some agreements." Tr. at 1299:21-1300:2 (Kightlinger); *see also* PTX-65 Recital D. The Transfer Agreement, as amended and signed at that Met ceremony, defines the "Actual Wheeling Rate" as the rate to be "determined by agreement or arbitration, litigation or other dispute-resolution mechanism" between San Diego and Met. PTX-28 at 119. It was common knowledge that San Diego had reserved its right to sue over Met's unlawful wheeling rates "at the end of the 5 years' QSA delay." PTX-81 (emphasis in original).

C. Mr. Kightlinger's counterfactual trial testimony

Nevertheless, Mr. Kightlinger testified at trial that San Diego agreed ***not*** to sue after five years—indeed, ***not for 45 to 75 years***—so long as Met did not change its "existing rate structure." Tr. at 1304:19-1307:2, 1320:21-1334:18, 1358:9-18, 1379:4-15 (Kightlinger). According to Mr. Kightlinger, he asked Ms. Stapleton and Mr. Slater "point blank" whether San Diego would challenge Met's "rate structure," and they answered that San Diego had "no objection to the rate structure," but only to "changes Metropolitan might make in the future," not the "existing rate structure." Tr. at 1304:19-1305:7 (Kightlinger). That is false. As Mr. Slater and Ms. Stapleton testified, they never told Mr. Kightlinger anything of the kind. *See* Tr. at 1176:6-1201:21 (Slater), 1519:24-1532:18, 1554:7-1562:22, 1563:10-1567:19 (Stapleton).

This is not simply a case of "he said, she said." This is "he said, ***everyone*** said"—***including Met itself in Phase I***. *See, e.g.*, Met's Oct. 18, 2013 Pretrial Br. at 14. In Phase I, Met admitted that "the threat of future litigation was made explicit by SDCWA in the context of negotiating" the Exchange Agreement. *Id.* And in the Exchange Agreement itself, San Diego "agreed not to challenge MWD's water rates for a period of five years after its execution. Thereafter, SDCWA reserved its right to challenge the validity of MWD's rates 'in an administrative or judicial forum.'" *Id.* San Diego's reservation of rights was in no way limited to "changes Metropolitan might make in the future," Tr. at 1304:19-1305:4 (Kightlinger), and Met

knows it. As Met admitted, San Diego "***openly threatened to litigate over MWD's existing rate structure***." Met's Oct. 18, 2013 Pretrial Br. at 14 (emphasis added).

June Skillman testified to the same effect in Phase I. Ms. Skillman was "the one who drafted the language" in Met's supposedly independent cost-of-service study, purporting to bless Met's existing rate structure as "appropriate." Tr. at 722:12-22 (Skillman). She admitted that she put that language in the cost-of-service study precisely because Met "expected to be sued because the only reason [San Diego] hadn't sued [Met] before was the 5-year standstill." *Id.* at 712:4-719:3; *see also id.* at 719:25-734:25 (Skillman).

Notably, Met never called Mr. Thomas to testify at trial, in either phase, even though Met named him Met's person most knowledgeable about the Exchange Agreement, and included him on its witness lists in both phases. Whatever Met's reasons for putting Mr. Thomas on its witness lists only to pull him at the last minute in both phases of trial, Met shut this particular barn door way too late. As discussed above, Mr. Thomas admitted at his PMK deposition that "***Section 5.2 allows the Water Authority to do what it has done in this case***." PTX-392 at 122:21-123:1 (emphasis added); *see id.* at 58:23-61:25; 121:10-127:5, 133:6-136:10, 143:4-11.

Met also never called Mr. Gastelum to testify, even though there is no reason to believe he was unavailable as a witness. *See* Tr. at 1038:11-16 (Cushman), 1525:13-16, 1555:20-1556:2 (Stapleton). Mr. Gastelum's contemporaneous communications, like Mr. Thomas's PMK deposition testimony, make clear that he also understood that San Diego had reserved its "right to challenge Metropolitan's uniform wheeling rates after five years from the date of execution of the QSA." PTX-80 (June 18, 2004). Likewise, on July 30, 2004, Mr. Gastelum sent a letter to Ms. Stapleton acknowledging "the reservation by the Authority in the Quantification Settlement Agreement (QSA) to challenge Metropolitan's rate structure after five years." DTX-909. And on November 18, 2004, Mr. Gastelum informed Met's member-agency managers that San Diego was "not willing to agree not to challenge Metropolitan's rate structure in a manner that would reduce Metropolitan's wheeling rate or Exchange Rate as defined in the QSA agreements." DTX-342. Nowhere in any of those memoranda (or anywhere else) did Mr. Gastelum suggest that San Diego had waived or otherwise failed to reserve its right to challenge Met's rates after five years, or that

any such challenge would be limited to procedural quibbles or changes to the "existing rate structure." On the contrary, Mr. Gastelum advocated Met's RSI clause precisely because of San Diego's "reservation" of its right "to challenge Metropolitan's rate structure after five years." DTX-909; *see also* PTX-80; DTX-342; PTX-95 at 2; Tr. at 1377:4-1378:21 (Kightlinger).

D. Met's breaches of the Exchange Agreement

The Court already knows, from Phase I, what happened between the execution of the Exchange Agreement and the filing of this lawsuit. That history was covered in San Diego's Phase I briefs and in the Court's Phase I opinion, which San Diego incorporates here by reference. *See, e.g.*, San Diego's First Pretrial Br. at 19-24; Reply at 3-5; Post-Trial Br. at 4-12; SOD at 40-44. In short, on April 13, 2010, Met adopted its rates for 2011 and 2012, over San Diego's objections. *See* AR2010-11203-214; AR2010-11343-92; AR-2010-11564-574. On April 10, 2012, Met adopted its rates for 2013 and 2014, again over San Diego's objections. *See* AR2012-16154-16241; AR2012-16995-17013; AR2012-17098-126.

Met's transportation rates for those years are unlawful, as the Court held in Phase I. *See* SOD. Met breached the Exchange Agreement by charging a Price consisting of those unlawful transportation rates rather than "charges set … pursuant to applicable law and regulation." PTX-65 § 5.2. Met concedes that San Diego "overpaid those charges." Tr. at 1911:25-1912:9 (Woodcock); *see also* SOD at 65 ("the record confirms that these rates over-collect from wheelers"); Tr. at 991:16-992:6 (Cushman). Met also does not dispute that San Diego performed all of its obligations under the Exchange Agreement. *See, e.g.*, Tr. at 987:1-7 (Cushman), 1365:9-13 (Kightlinger); PTX-177; PTX-225.

E. San Diego's damages: $188,295,602, plus interest

San Diego's damages expert, Dan Denham, testified that San Diego's damages are $188,295,602, plus interest. *See* Tr. at 1104:16-1120:17 (Denham); PTX-471; PTX-508-12. Mr. Denham calculated San Diego's damages by removing SWP costs and the Water Stewardship Rate from the Price Met charged under the Exchange Agreement from 2011 to 2014. Those charges do not belong in the Price because Met did not set them "pursuant to applicable law and regulation." PTX-65 § 5.2; *see also* SOD at 53-61, 65; Tr. at 303:12-314:25, 1104:10-1120:18

(Denham); PTX-471; PTX-508-512.

Specifically, for 2011, the Price Met actually charged San Diego under the Exchange Agreement (consisting of Met's transportation rates) was $372/AF. Tr. at 311:13-18 (Denham); PTX-508. Of that Price, the overcharge—the unlawful SWP charges and Water Stewardship Rate—was $236/AF. Tr. at 311:7-25, 1113:19-1114:13 (Denham); PTX-471; PTX-508. Removing that overcharge from the actual Price gives the corrected wheeling rate of $136/AF. Tr. at 303:12-311:21 (Denham). And multiplying the $236/AF overcharge by the 143,242.90 acre feet Met transported to San Diego and charged San Diego for under the Exchange Agreement in 2011 yields the total overcharge for 2011: $33,805,324. Tr. at 1106:23-1115:3 (Denham); PTX-471; PTX-508.[12]

For 2012, the corrected wheeling rate is $164/AF. Tr. at 312:6-313:12 (Denham). Met's actual Price was $396/AF and it overcharged San Diego by $232/AF. The exchange volume for 2012 was 186,861 AF. The total 2012 overcharge, therefore, was $43,351,752. Tr. at 1115:4-1116:16 (Denham); PTX-471; PTX-509.

For 2013, the corrected wheeling rate is $138/AF. *Id.* at 313:21-314:6 (Denham). Met's actual Price was $453/AF and it overcharged San Diego by $315/AF. The exchange volume for 2013 was 180,256 AF. The total 2013 overcharge, therefore, was $56,780,640. Tr. at 1116:21-1118:3 (Denham); PTX-471; PTX-510.

And for 2014, the corrected wheeling rate is $143/AF. Tr. at 314:14-23 (Denham). Met's actual Price was $445/AF and it overcharged San Diego by $302/AF. The exchange volume for 2014 was 179,993 AF. The total 2014 overcharge, therefore, was $54,357,886. Tr. at 1118:8-1119:11 (Denham); PTX-471; PTX-511.

San Diego's damages of $188,295,602 are the sum of these overcharges from 2011 to 2014. Tr. at 1119:13-1120:17 (Denham); PTX-471; PTX-512. To be clear, San Diego has not asked for a complete refund of the Price it paid Met to convey San Diego's water under the Exchange Agreement. San Diego does not challenge in this case the amounts Met charged for the

[12] The exchange volume was rounded up to 143,243 in PTX-508, but the annual overcharge of $33,805,324 is based on the actual exchange volume of 143,242.90 AF. *See id.*; PTX-471.

fixed costs of the Colorado River Aqueduct and Met's internal distribution system, or the power costs associated with Met's systems (as opposed to DWR's SWP). Even after the unlawful components of Met's Price are removed, San Diego still paid Met $100,740,565 in conveyance charges under the Exchange Agreement, for 2011 to 2014 alone, which San Diego did not dispute in this case. *See* PTX-512. San Diego also paid another $130,955,080 in undisputed charges under the Exchange Agreement from 2004 to 2010, before San Diego brought this suit, and still another $5.7 million for a separate wheeling transaction that San Diego did not challenge. *See* PTX-473. San Diego has made all of those payments over the years, along with its payments to IID, starting at $250/AF (currently at $624/AF), with no contribution from any of Met's other member agencies, even though Director Kennedy, for example, expressly found—pursuant to emergency legislative mandate and the Wheeling Statutes—that San Diego should have received at least $220/AF back from Met and its other member agencies for San Diego's crucial investments in conservation and a full Colorado River Aqueduct. *See* PTX-481 n.3; *see also* Water Code § 1811(c); S.B. 1082; PTX-24-26; PTX-30. The evidence shows that San Diego's proven damages of $188,295,602 are not only reasonable, but conservative.

IV. ARGUMENT

A. Met's liability is established and its motion for partial judgment is meritless.

There is no legitimate dispute that San Diego proved Met's liability for breaching the Exchange Agreement. The elements of a cause of action for breach of contract are "a contract, plaintiff's performance or excuse for failure to perform, defendant's breach and damage to plaintiff resulting therefrom." *McKell v. Washington Mut., Inc.*, 142 Cal. App. 4th 1457, 1489 (2006). As discussed above, Met does not dispute the existence of the Exchange Agreement or San Diego's performance of it. *See, e.g.*, Tr. at 987:1-7 (Cushman). Given the Court's Phase I decision, Met also cannot seriously dispute that it breached the Exchange Agreement and thereby caused damage to San Diego. *See* SOD at 65; Tr. at 991:16-992:6 (Cushman), 1911:25-1912:9 (Woodcock); *McKell*, 142 Cal. App. 4th at 1489-90 (unlawful fees are a breach of contract); *Bird, Marella, Boxer & Wolpert v. Superior Court*, 106 Cal. App. 4th 419, 427 (2003) (plaintiffs have

"the right not to be subjected to … unlawful billing practices").[13]

Nevertheless, in its motion for partial judgment, Met argues that San Diego did not prove breach because San Diego "paid exactly what it proposed and agreed to pay: State Water Project costs and the Water Stewardship Rate." MPJ at 3. But that is ***not*** what San Diego agreed to pay, as Met admits on the same page. *See id.* What San Diego agreed to pay, after the first year when the Price was set at $253/AF, were "conveyance charges set pursuant to 'applicable law and regulation.'" *Id.* (quoting PTX-65 § 5.2).

Met tries to escape the plain meaning of the parties' agreement by means of an argument in the form of a *reductio ad absurdum*. Met contends that because the "same rates and cost components that were used the first year of the agreement were used every year thereafter," this must mean that San Diego agreed "to the lawfulness of the charges … for up to forty-five years" because otherwise the Exchange Agreement would have been "void *ab initio*." *Id.* at 3-4. But Met's *reductio* fails because Met admits, in the same breath, that "nothing prohibits contracting parties from agreeing that as between them, these charges are fair and reasonable and will be the price of the contract." *Id.* at 3. That is what San Diego and Met did in agreeing to the $253/AF rate for the first year—but ***only*** the first year. *See* PTX-65 § 5.2; *see also, e.g.*, Tr. at 1008:23-1009:06 (Cushman), 1596:9-1597:17 (Stapleton). "***Thereafter***, the Price shall be equal to the charge or charges set by Metropolitan's Board of Directors pursuant to applicable law and regulation and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2 (emphasis added). Although San Diego still could not

[13] In its motion for partial judgment, Met emphasizes that Mr. Cushman stated that he did not "'know whether San Diego would necessarily be better off under some [unspecified] alternative rate structures.'" MPJ at 6 (quoting Tr. at 1047:25-1048:5). But Mr. Cushman testified that he is not aware of "any rate structure proposal consistent with cost causation principles that would have charged San Diego more money" or, indeed, "any way" that Met could have charged its SWP costs to its transportation rates "consistent with cost causation principles." Tr. at 1099:16-1100:3 (Cushman); *see also id.* at 1052:2-22. Whatever Met might have charged based on some unspecified alternative rate structure that it never considered, adopted, or proved lawful, the Court's Phase I ruling establishes that Met's actual rates are unlawful, and that San Diego "therefore stated a cause of action for breach of contract." *McKell*, 142 Cal. App. 4th at 1490.

challenge the rates for another four years because of the "five-year cooling off period,"[14] San Diego retained "the ability to challenge the rates under applicable law after the end of that period." Dec. 4, 2013 Order at 4 n.9; *see also, e.g.*, *Salmon Prot. & Watershed Network v. Cnty. of Marin*, 205 Cal. App. 4th 195, 202 (2012) (holding that a public agency may agree to toll the time to bring an action challenging compliance with the law).

Met also contends that the provision that "nothing herein shall preclude" San Diego from challenging "such charge or charges" after five years only refers to the preceding statement "that Metropolitan may at any time amend the Administrative Code." PTX-65 § 5.2; *see* MPJ at 5. But Met's interpretation robs the phrase "nothing herein" of its plain meaning and, in any event, Met's reservation of its right to amend its Administrative Code does not even contain the phrase "charge or charges." PTX-65 § 5.2. The antecedent of "charge or charges" is the crucial provision that "the Price shall be equal to the charge or charges set by Metropolitan's Board of Directors pursuant to applicable law and regulation and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." *Id.* That is what San Diego retained the right to challenge after five years, which "nothing herein shall preclude." *Id.*; *see also*, *e.g.*, Dec. 4, 2013 Order at 3-5; Tr. at 1609:6-16 (Stapleton).

Met cites *Coughlin v. Blair*, 41 Cal. 2d 587, 602 (1953), for the proposition that if "'the injured party accepts or urges performance by the promisor, he will not be allowed to obtain damages on the theory that performance has not been made.'" MPJ at 6. But the issue in *Coughlin* was "whether ***defendants*** should receive credit for performance after the complaint was filed." 41 Cal. 2d at 602 (emphasis added). The Court held that the defendants should not receive any such offset because the plaintiffs "did not urge performance after the complaint was filed, and they could not prevent it," and "such gratuitous benefit, wholly speculative on the record, would not constitute unjust enrichment to plaintiffs." *Id.* at 602-03. *Coughlin* is only relevant here because, under *Coughlin* and the Court's Phase I decision, Met cannot claim any

[14] Met disparages the phrase "'cooling off' period," MPJ at 3, but that phrase comes from the Court's December 4, 2013 Order, and is consistent with the "peace treaty" language the parties used in negotiations. *See, e.g.*, PTX-58 ¶ 8; Dec. 4, 2013 Order at 4-5 n.9.

offset or unjust enrichment based on blending. *See id.*; SOD at 53; § IV.C, *infra*. Furthermore, Met cannot reasonably contend that San Diego ever "urge[d]" Met to impose unlawful rates. *Coughlin*, 41 Cal. 2d at 602. On the contrary, San Diego did everything it could to prevent Met from doing so. For the same reason, Met's assertion that San Diego's "conduct for many years was entirely consistent with the understanding that it had a permanent deal on the price," MPJ at 5, is false. In fact, as discussed at length above and as Met itself admitted in Phase I, San Diego "openly threatened to litigate over MWD's existing rate structure." Met's Oct. 18, 2013 Pretrial Br. at 14; *see also* §§ III.A-D & n.4, *supra*.

Met concludes by citing *California Lettuce Growers v. Union Sugar Co.*, 45 Cal. 2d 474 (1955), for the proposition that San Diego is stuck with Met's rates for 45 to 75 years even though those rates are "'unilateral and unfair.'" MPJ at 6 (quoting 45 Cal. 2d at 481). Not only is that a misinterpretation of *California Lettuce*, it is at odds with Met's arguments against San Diego's supposedly "unilateral" position in the context of Section 12.4(c), and directly contradicts the Court's Order regarding Section 12.4(c), which held, at Met's behest, that "***Met is required to perform the contract by setting a lawful price***." Nov. 4, 2014 Order re Damages at 10 (emphasis added). Having won that argument, Met is judicially estopped from arguing otherwise now. *See, e.g.*, *Jackson v. Cnty. of Los Angeles*, 60 Cal. App. 4th 171, 183 (1997).

Thus, the Court should deny Met's motion for partial judgment. Met's liability for breaching the Exchange Agreement is established.

B. Met's affirmative defenses have no legal or evidentiary merit and must fail.

1. Met's affirmative defenses of waiver, consent and estoppel fail.

Like Met's motion for partial judgment, Met's affirmative defenses of waiver, consent and estoppel founder on the express terms of the Exchange Agreement. As discussed above, the Court already held that the fact that "San Diego paid its bills under the contract and did not bring a legal challenge to the 2003-2007 rates … is not a concession that the rates complied with law, only that San Diego was complying with the five year hiatus agreement," which "supports the inference that San Diego intended to retain the ability to challenge [Met's] rates under applicable law after the end of that period." Dec. 4, 2013 Order at 4 & n.9. Met's affirmative defenses fail,

therefore, because "written contracts cannot be set aside and implied agreements substituted therefor if the conduct of the parties was not clearly contrary to the terms of the written contract." *Garrison v. Edward Brown & Sons*, 25 Cal. 2d 473, 480 (1944); *see also* PTX-65 § 13.6 (integration clause). As detailed above, far from "consenting" to pay Met's unlawful rates for 45 to 75 years, San Diego expressly reserved its right to challenge them after five years; repeatedly attempted to convince Met to change them through Met Board and Committee processes; and then, when everything else had failed, sued Met to invalidate its rates and for damages, precisely as Met's PMK witness Brian Thomas admitted "Section 5.2 allows the Water Authority to do … in this case." PTX-392 at 122:21-123:1 (Thomas).

The Exchange Agreement's anti-waiver provisions also defeat Met's defenses:

> [T]he non-breaching Party will have all rights and remedies provided at law or in equity against the breaching Party.…
>
> If the non-breaching Party fails to exercise or delays in exercising any such right or remedy, the non-breaching Party does not thereby waive that right or remedy. In addition, no single or partial exercise of any right, power, or privilege precludes any other or further exercise of a right, power, or privilege granted by this Agreement or otherwise.…
>
> No waiver of a breach, failure of condition, or any right or remedy contained in or granted by the provisions of this Agreement is effective unless it is in writing and signed by the Party waiving the breach, failure, right, or remedy. No waiver of a breach, failure of condition, or right or remedy is or may be deemed a waiver of any other breach, failure, right or remedy, whether similar or not. In addition, no waiver will constitute a continuing waiver unless the writing so specifies.

PTX-65 §§ 12.3, 12.5, 13.9. ***Met admits that there is no writing establishing any waiver by San Diego, much less a continuing one.*** *See* Tr. at 1337:21-1339:6 (Kightlinger); *see also* Tr. at 1201:17-21 (Slater).

Thus, Met's affirmative defenses of waiver, consent and estoppel fail under the express terms of the Exchange Agreement and Met's own admissions. Met's affirmative defenses also fail as a matter of law because Met has a continuing legal obligation to charge lawful transportation rates and a lawful Price. *See, e.g.*, *Barratt Am. Inc. v. City of Rancho Cucamonga*, 37 Cal. 4th 685, 703-04 (2005); *Arcadia Dev. Co. v. City of Morgan Hill*, 169 Cal. App. 4th 253, 262-64 (2008); *McKell*, 142 Cal. App. 4th at 1489-90; *Bird*, 106 Cal. App. 4th at 427. Every unlawful charge "was a new breach of the contract, and the fact that plaintiff may have waived

the breach up to a given time did not preclude him from asserting a subsequent breach." *Woodard v. Glenwood Lumber Co.*, 171 Cal. 513, 523 (1915). Again, San Diego never waived any breach, *see* §§ III.B-D & IV.A, *supra*, but even if it had, Met cannot assert—and certainly has not carried its burden of proving—that San Diego waived, consented to, or is estopped from asserting Met's breaches arising from the unlawful charges at issue in this case: the invalid transportation rates Met set in 2010 and 2012, which it wrongfully charged as its Exchange Agreement Price from 2011 to 2014. *See* PTX-65 §§ 12.3, 12.5, 13.9; AR2010-11203-214; AR-2010-11564-574; AR2012-16154-16241; AR2012-16995-17013; *Woodard*, 171 Cal. at 523.

2. Met's illegality and mistake defenses also fail.

The premise of Met's illegality defense is that the Exchange Agreement is illegal because Met's rates are illegal. But it is "well settled that if a contract can be performed legally, it will not be presumed that the parties intended for it to be performed in an illegal manner, and it will not be declared void merely because it was performed in an illegal manner." *Freeman v. Jergins*, 125 Cal. App. 2d 536, 546 (1954). Met certainly ***could*** have charged a lawful Price. Indeed, as discussed below, it could have charged the corrected wheeling rates that are the basis for San Diego's calculation of damages. *See* § IV.C, *infra*.[15]

Met's "mistake of law" defense requires Met to prove a "misapprehension of the law by all parties, all supposing that they knew and understood it, and all making substantially the same mistake as to the law," or a "misapprehension of the law by one party, of which the others are aware at the time of contracting, but which they do not rectify." Civ. Code § 1578. Where, as here, the parties disagreed about the law when they entered into the contract, the risk that one or the other might later be proven wrong is "an element of the bargain. Otherwise stated, the kind of mistake which renders a contract voidable does not include mistakes as to matters which the contracting parties had in mind as possibilities and as to the existence of which they took the risk." *Stermer v. Bd. of Dental Examiners*, 95 Cal. App. 4th 128, 134 (2002) (citations and

[15] Moreover, if the Exchange Agreement were illegal (which it is not), San Diego would be entitled to a full refund of all consideration, whereas Met would be barred as a matter of law from seeking any offset. *See, e.g., R. M. Sherman Co. v. W. R. Thomason, Inc.*, 191 Cal. App. 3d 559, 563 (1987); *Marshall v. La Boi*, 125 Cal. App. 2d 253, 268 (1954).

quotation marks omitted). Likewise, where—again, as here—the defendant attempts to rely on its own "purported misunderstanding" of the contract as an alleged "mistake of law," the defense fails. *Dowling v. Farmers Ins. Exch.*, 208 Cal. App. 4th 685, 699 (2012). "This does not constitute a 'mistake' for rescission purposes." *Hedging Concepts, Inc. v. First Alliance Mortgage Co.*, 41 Cal. App. 4th 1410, 1421 (1996). Here, as already discussed several times, San Diego and Met disagreed about the law all along and San Diego tried to rectify Met's illegal rates, but Met insisted on imposing them over San Diego's objections, and thus knowingly took the risk that its rates would be found invalid, as they now have been. *See* §§ III.A-D & n.4, *supra*; SOD.

Thus, Met's affirmative defenses have no legal or evidentiary merit and must fail.

C. The Court should award San Diego $188,295,602 in damages, plus interest.

Because Met's liability is established and its affirmative defenses fail, as discussed above, the Court should award damages to San Diego based on the measure that is "most definite and certain," and "best achieves the fundamental purpose of compensation." *A. A. Baxter Corp. v. Colt Indus., Inc.*, 10 Cal. App. 3d 144, 160 (1970); *see also, e.g.*, Nov. 4, 2014 CMC Order at 2 n.2 (citing *Meister*). San Diego proved that it is entitled to $188,295,602 in damages, plus interest. Met proved nothing.

In determining contract damages, "California law requires only that some reasonable basis of computation be used, and the damages may be computed even if the result reached is an approximation." *SCI Cal. Funeral Servs., Inc. v. Five Bridges Found.*, 203 Cal. App. 4th 549, 570 (2012) (quotation marks and ellipses omitted). "This is especially true where, as here, it is the wrongful acts of the defendant that have created the [purported] difficulty in proving the amount" of damages. *GHK Assocs. v. Mayer Group, Inc.*, 224 Cal. App. 3d 856, 874 (1990); *accord Meister*, 230 Cal. App. 4th at 397. "The most elementary conceptions of justice and public policy require that the wrongdoer shall bear the risk of the uncertainty which his own wrong has created. That principle is an ancient one.'" *Allen v. Gardner*, 126 Cal. App. 2d 335, 340 (1954) (ellipses omitted) (quoting *Bigelow v. RKO Radio Pictures*, 327 U.S. 251, 265 (1946)). Where, as here, the fact of damages is proven and the plaintiff offers a reasonable computation of the amount of damages, the "'burden rests upon the defendant'" to prove that

those damages should be "'reduced'" or otherwise offset. *Meister*, 230 Cal. App. 4th at 397 (quoting *Fibreboard Paper Prods. Corp. v. East Bay Union of Machinists*, 227 Cal. App. 2d 675, 705 (1964)); *Space Properties, Inc. v. Tool Research Co.*, 203 Cal. App. 2d 819, 827 (1962) ("Since a defense in the nature of unjust enrichment or setoff is clearly an affirmative one, the burden" is on the party asserting the defense); *Conrad v. Ball Corp.*, 24 Cal. App. 4th 439, 444 (1994) (same). To hold otherwise would violate the principle that "[n]o one can take advantage of his own wrong." Civ. Code § 3517.[16]

Leading up to the Phase II trial, the parties debated the proper measure of damages. San Diego contended, and still contends, that damages should be measured by removing the charges Met never had any legal or contractual basis for including in the Price—SWP costs and the Water Stewardship Rate. San Diego's measure of damages follows from the Exchange Agreement and California damages law, and is further supported by tax-refund cases—especially given that, under the Court's Phase I decision, Met's unlawful charges are taxes. *See generally* San Diego's Phase II Pretrial Br.[17] Met, on the other hand, argued that the only proper measure of damages is the difference between the Price Met actually charged and the "highest lawful rate"—a measure that, as San Diego pointed out, is contrary to California law, including the Wheeling Statutes, and has been expressly rejected by the federal courts. *See id.*[18]

After trial, the parties' pretrial debates over the measure of damages have become somewhat academic because it is now clear that under ***any*** measure, San Diego is entitled to ***at***

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[16] *See also, e.g., Ward v. Taggart*, 51 Cal. 2d 736, 744 (1959); *Kashmiri v. Regents of Univ. of Calif.*, 156 Cal. App. 4th 809, 849 (2007); *Brandon & Tibbs v. George Kevorkian Accountancy Corp.*, 226 Cal. App. 3d 442, 458-59 (1990); *DePalma v. Westland Software House*, 225 Cal. App. 3d 1534, 1544-46 (1990); *C. Norman Peterson Co. v. Container Corp. of America*, 172 Cal. App. 3d 628, 646-47 (1986); *A&M Records, Inc. v. Heilman*, 75 Cal. App. 3d 554, 570-71 nn.11-12 (1977); *Benard v. Walkup*, 272 Cal. App. 2d 595, 605-06 (1969); *Milton v. Hudson Sales Corp.*, 152 Cal. App. 2d 418, 434-36 (1957).

[17] *See also, e.g., Shapell Indus., Inc. v. Governing Bd.*, 1 Cal. App. 4th 218, 244 (1991); *Gen. Motors Corp. v. San Francisco*, 69 Cal. App. 4th 448, 454-55 (1999); *Warmington Old Town Associates, L.P. v. Tustin Unified Sch. Dist.*, 101 Cal. App. 4th 840, 867 (2002); *City of Modesto v. Nat'l Med, Inc.*, 128 Cal. App. 4th 518, 525-28 (2005); *Cresta Bella, LP v. Poway Unified Sch. Dist.*, 218 Cal. App. 4th 438, 453 (2013).

[18] *See also, e.g., Oneida Motor Freight, Inc. v. I.C.C.*, 45 F.3d 503, 507-08 (D.C. Cir. 1995); *MCI Telecommunications Corp. v. F.C.C.*, 59 F.3d 1407, 1415-19 (D.C. Cir. 1995).

least $188,295,602 in damages. As discussed above, San Diego's damages are measured by the difference between the Price Met actually charged and what it could have charged based on the corrected wheeling rates—between $136/AF and $164/AF—that Mr. Denham calculated by removing the unlawful and contractually-prohibited SWP costs and Water Stewardship Rate. *See* Tr. at 303:12-314:25, 1104:10-1120:18 (Denham); PTX-471; PTX-508-512. There is no legitimate question that Mr. Denham properly removed those charges. Met's damages expert, Mr. Woodcock, admitted that Mr. Denham's "math was proper," Tr. at 1916:19, and Messrs. Woodcock and Upadhyay further conceded that Met's conveyance of water under the Exchange Agreement does not cause Met to incur ***any*** SWP costs, or ***any*** of the demand-management costs for which Met imposes the Water Stewardship Rate. Tr. at 1933:2-18 (Woodcock), 1428:25-1429:7 (Upadhyay). Met presented no admissible evidence to prove that it could lawfully include ***any*** of those charges in its Price under the Exchange Agreement, and Met's criticisms of San Diego's proven damages are meritless.

Met's argument, in its motion for partial judgment, that "[w]ithout evidence of a price that could have been set, SDCWA has not proved damages," MPJ at 7, fails because San Diego not only presented evidence of Prices Met could have set, San Diego's evidence stands unrebutted. Met certainly could have set wheeling rates, and therefore Prices under the Exchange Agreement, between $136/AF and $164/AF, just as Mr. Denham testified. For example, Director Kennedy found, pursuant to the Wheeling Statutes and the Legislature's mandate, that $80/AF would be a perfectly fair wheeling rate, taking "into account Metropolitan's fixed system costs and the regional benefits provided by San Diego bringing conserved IID water to the region," and consistent with "a more generic analysis" that would apply to "Metropolitan and any of its member agencies." PTX-481. In other words, according to Director Kennedy—and as Met itself effectively conceded at the time, *see* AR2010-2972 at 2977—Met could have charged $80/AF as the Exchange Agreement Price "pursuant to applicable law and regulation and generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2. Met's Board agreed to use the $80/AF wheeling rate as the basis for the rates in the 1998 Exchange Agreement, which would have set the wheeling rates for 2011 to 2014 between

$109.92/AF and $115.11/AF—well below the corrected wheeling rates Mr. Denham calculated at between $136/AF and $164/AF. *Compare* PTX-31 Ex. 1 *with* PTX-471.

Although Met likes to claim that the wheeling rates in the 1998 Exchange Agreement were "discounted" and would only have been fair if Met had received the canal-lining money—even though Met refused to take on the countervailing risks and responsibilities, *see, e.g.*, PTX-65 § 10.7—the premise of Met's argument is that it was right all along to include its SWP costs and Water Stewardship Rate in its wheeling rates. *See, e.g.*, Tr. at 1288:13-1290:4 (Kightlinger). But Met was ***wrong*** all along, as the Court has already found. *See* SOD at 52-61, 65. Indeed, Met was wrong in ways this Court has yet to address. In particular, without what Met misleadingly labels a "discount"—which is, in reality, nothing more than the reasonable credit Director Kennedy rightly found to be necessary and appropriate under the Wheeling Statutes—Met's wheeling rates unlawfully deny San Diego any credit for the undeniable "offsetting benefits for the use of the conveyance system" to convey conserved IID water to the coastal plain of Southern California. Water Code § 1811(c); *see, e.g.*, PTX-24-26; PTX-30; PTX-481.

Indeed, by Met's own reasoning, it should have charged all of its member agencies, not just San Diego, for the established regional benefits of San Diego's conserved IID and canal-lining water. During closing arguments in Phase I, the Court pointed out that "under [Met's] reasoning," even if Met "had one project, just a single project that costs a tremendous amount of money," but "generated water for only" one member agency, Met "would just say, well, the fact that one member agency is now using this water is, at least, indirectly something that benefits everybody. So therefore, every member agency is going to be picking up this tab." Tr. at 946:24-947:18 (Court). Although Met's counsel tried to resist the Court's hypothetical, he ultimately agreed: "That's right." *Id.* at 948:4.

Met's argument that it should be allowed to charge all of its member agencies for benefits that go to only one member, or for purported regional benefits that Met has never even tried to prove or quantify, is wrong for the reasons the Court already recognized in Phase I. But it is important to remember Met's argument because it highlights the irrationality of Met's discrimination against San Diego. Instead of setting a wheeling rate that gives San Diego credit,

as the Wheeling Statutes require, for regional benefits that Met admits exist, and which both Met and Director Kennedy quantified, Met loads up its wheeling rate with SWP costs that admittedly have nothing to do with wheeling. *See* Tr. at 1933:2-18 (Woodcock). Met also includes the Water Stewardship Rate as a wheeling charge, when it is really nothing more than a tax, and is admittedly unrelated to wheeling. *See* Tr. at 1418:14-18, 1428:25-1429:7 (Upadhyay), 1910:10-1913:20 (Woodcock). By including its unlawful Water Stewardship Rate in its Exchange Agreement Price, Met also forces San Diego to pay for all of the other member agencies' local water projects, the supposed benefits of which Met has never tried to prove or quantify, while simultaneously failing to give San Diego any credit for the regional benefits Met itself, and Director Kennedy, directly attributed to the IID-San Diego transfer. What's more, Met denies San Diego any proportionate benefit from the unlawful Water Stewardship Rate, just because San Diego brought this lawsuit to prove that what Met is doing is unlawful, which it is. *See, e.g.*, Tr. at 201:9-206:4, 1013:4-1017:5 (Cushman); PTX-506; SOD. And to top it all off, Met now claims, in this litigation, that San Diego will be "unjustly enriched" by the modest damages San Diego seeks, when in fact, San Diego's contract damages will only partly compensate it for the unjust enrichment Met's other member agencies have obtained over the years, at San Diego's expense. *See* Tr. at 1014:20-1017:9 (Cushman), 1123:21-1125:23 (Denham), 1648:14-21 (Stapleton); PTX-171; PTX-473; PTX-506. This is Kafka, not cost causation.

Similarly, at trial, Mr. Woodcock criticized Mr. Denham because when Denham calculated corrected wheeling rates, he did not take it upon himself to also calculate new supply rates. *See* Tr. at 1895:24-1899:7, 1905:17-1916:24 (Woodcock); *see also* MPJ at 8-9. But the supply rate is not part of Met's wheeling rate, thus is not part of the Price, and therefore is not part of the corrected wheeling rate and not part of Mr. Denham's damages analysis. To the extent Mr. Woodcock's argument is simply that, given the corrected wheeling rates, "Metropolitan must recover its costs somewhere," he admitted that "the money in the escrow could be used to pay damages in this case without anybody changing any rates for those four years." Tr. at 1914:3-21 (Woodcock). Indeed, under the Court's interpretation, the purpose of Section 12.4(c) is "to ensure that disputed funds were promptly available to the prevailing party upon the resolution of a

dispute." Nov. 4, 2014 Order re Damages at 7.

To the extent Met contends that San Diego's damages should be offset by increased supply rates, or that San Diego would be unjustly enriched if it is not required to pay increased supply rates, it was Met's burden to prove any such purported offset or unjust enrichment. *See, e.g.*, *Meister*, 230 Cal. App. 4th at 397; *Space Properties*, 203 Cal. App. 2d at 827. To require San Diego to calculate such a supply rate "would be to ask of it the very thing that [Met] was itself unable to do," which would be both "inequitable" and "absurd." *MCI*, 59 F.3d at 1415. Given that Met, "with its superior information, could not (or did not) accurately establish such a rate, then it seems obvious that [San Diego] could not (or should not be expected to) establish such a rate from the outside looking in." *Id.* Indeed, not only did Met fail to prove any offset or unjust enrichment, Mr. Woodcock admitted that any attempt to do so on the basis of purported supply-rate increases would be inherently speculative and counterproductive because Met might not have increased its supply rates at all. *See* Tr. at 1916:25-1929:13 (Woodcock). Met might have chosen to raise property taxes instead, for example. *Id.* at 1929:3-9. Twelve "experts would come up with 12 different ways to do it," and it "is impossible to know what the board might do with their rates given the Court's ruling." *Id.* at 1929:7-13. Whatever Met might have done, or will do, it cannot make San Diego wait for Met to figure things out, much less force San Diego to figure them out, after all these decades of Met refusing to listen. *See, e.g.*, *Meister*, 230 Cal. App. 4th at 397; *MCI*, 59 F.3d at 1415; PTX-65 § 12.4(c); Nov. 4, 2014 Order re Damages at 7.

Met's offset theory also violates the statutory requirement that rates "shall be uniform for like classes of service throughout the district." Water Code § 109-134. As the court held in *MCI*, awarding an offset for a ***different*** rate in the context of determining damages for the unlawfully-inflated rates "effectively allows [San Diego] alone to be charged for the offsetting category of service at a rate above what others paid for it," which "is inconsistent with the statutory and regulatory goal of preventing discrimination." *MCI*, 59 F.3d at 1419; *see* Water Code § 109-134. None of Met's other member agencies paid the increased supply rate that Mr. Woodcock speculated about but was unable or unwilling or simply unprepared to calculate. San Diego, therefore, cannot be required to pay that hypothetically increased supply rate, either—as a matter

of law, *see id.*, and also as a practical matter because nobody knows what it is. In fact, it would be even more unfair here than in *MCI* to require San Diego to pay some special supply rate that Met's other member agencies have never paid, because ever since 2003, when conserved IID water that San Diego paid for began to be transferred under the long-awaited plan "to maintain a full Colorado River Aqueduct," Met's other member agencies have benefitted from artificially low supply rates at San Diego's expense. PTX-25; *see also, e.g.*, PTX-171; PTX-481.

Mr. Woodcock's only other criticism of Mr. Denham's analysis was that the corrected wheeling rates were calculated using Met's total annual water deliveries as the denominator. *See* Tr. at 1899:10-1900:14 (Woodcock). But in order to calculate a rate that will be charged on all water Met delivers—which is how Met charges its transportation rates—Mr. Denham ***had*** to use total Met water deliveries as the denominator. *See* Tr. at 1143:4-25, 1145:16-1146:3, 1151:2-5 (Denham). Otherwise, as Mr. Woodcock admitted, Mr. Denham would have been creating a "new rate structure"—for example, one "limited to Colorado River sales." Tr. at 1929:14-1930:17 (Woodcock). Again, it would be "inequitable" and "absurd" to require San Diego to develop and defend an entirely "new rate structure," *id.*, when that is "the very thing that [Met] was itself unable to do." *MCI*, 59 F.3d at 1415.

Moreover, the "new rate structure" Mr. Woodcock suggested would be based on whatever "blend" of SWP water Met happens to provide. *See* Tr. at 1874:11-1875:9, 1903:4-25, 1930:23-1937:25, 1941:10-1942:4 (Woodcock). But the Court already rejected this argument. Again, it "does [not] matter whether Met delivers a blend of water to wheelers. The blend might be useful but, as to wheelers, the benefit is gratuitous, and not required by wheeling agreements." SOD at 53 (citations and footnotes omitted); *see also Coughlin*, 41 Cal. 2d at 602-03 (defendants are not entitled to an offset and cannot assert unjust enrichment based on "gratuitous" benefits). More generally, Mr. Woodcock's testimony is fundamentally incompatible with the Court's Phase I ruling that Met cannot charge SWP costs to transportation because they are not "***Met's*** transportation costs, any more than the overhead or payroll costs of Ford Motor Company are the overhead or payroll costs of a customer who buys a Ford car." SOD at 53 (emphasis in original). For Met, SWP costs are supply costs. Indeed, Met previously "allocated SWP costs to supply,

and ***none*** to transportation (including the SWP costs that DWR bills as its own transportation costs). No reasonable basis appears in the record as to why this has changed." *Id.* (emphasis added). After trial, there is still no reasonable basis for Met to include ***any*** SWP costs in its wheeling rate, based on blending or otherwise. Met certainly did not provide any such proof. Nor could it—SWP costs are supply costs. *See id.* (And, again, Met did not even try to argue that there is any lawful basis for it to charge any portion of its Water Stewardship Rate.)

Furthermore, the Exchange Agreement gives Met "sole discretion" over the blend it provides, and states that "in no event shall SDCWA be deemed to have any right to receive Exchange Water of better quality than the Conserved Water and/or Canal Lining Water." PTX-65 §§ 1.1(m), 3.2(e), 3.6; *see also, e.g.*, Tr. at 1568:5-1570:13 (Stapleton); 1688:5-1701:16 (Yamasaki), 1934:16-1935:21 (Woodcock). In fact, the "Bureau of Reclamation actually has the [Exchange] water available at the beginning of each water year, and … allows Met to take that water uniformly, and then at the end of the year, they do the accounting and true it up." Tr. at 1570:14-1571:17 (Stapleton); *see also, e.g.*, Tr. at 617:11-623:19 (Upadhyay), 1091:9-24 (Cushman), 1313:18-1314:5 (Kightlinger). Met asked to be allowed to convey that water to San Diego in "equal allocations" for Met's own "operational purposes." Tr. at 1567:20-1568:4 (Stapleton). Because determining the amount and quality of the Exchange Water is really just a matter of accounting, nothing prevents Met from accounting for all of it as Colorado River water—especially because Exchange Water, by definition, must be of "like quality" to Colorado River water, and Met is not required to provide San Diego with any more Exchange Water than Met actually receives from the Colorado River. PTX-65 art. III, §§ 1.1(m) & (r); *see also, e.g.*, Tr. at 1688:5-1701:16 (Yamasaki), 1948:24-1954:4 (Woodcock).

Mr. Woodcock's hypothetical blend-based rate also would "change all the time," based on what Mr. Woodcock referred to as Met's "big black box where you have water coming from two sources and going out to 26 different agencies." Tr. at 1874:11-1875:9, 1903:4-25, 1930:23-1937:25 (Woodcock). Thus, it would be "necessary to have different rates for different blends," which would fluctuate on a "monthly basis," if not "every day, every week and every hour." *Id.* at 1937:1-8, 1941:25-1942:4. But rates that fluctuate according to the accidents of hydrology,

geography, and Met's discretion would only exacerbate the problems that have plagued Met for half a century—opacity in its charges combined with instability in its rates, with the result that there is "'little basis for [Met's] constituent members to evaluate pricing problems except in terms of seeking the greatest individual advantage for each member,'" and Met "does not have the stable markets enjoyed by most water supplying agencies." PTX-6 (1969 Study) at 7, 245 (quoting 1968 Report of Assembly Committee on Water).

In fact, the stochastic rates Mr. Woodcock proposed would violate the very ratemaking principles he elsewhere espouses. The American Water Works Association ("AWWA") M-1 Manual, to which Mr. Woodcock contributed and on which he based his testimony,[19] emphasizes the importance of stability and predictability in rates: "Many of the desired outcomes of a rate structure depend on customers receiving a price signal." AR2010-3865 at 3967. By definition, however, the only "signal" one receives from a "black box" is its output—which, in the case of a blend-based system, would necessarily be unstable and unpredictable. *See* Tr. at 1937:1-25, 1941:10-1942:4 (Woodcock). This would be a problem not only for San Diego, but for all of Met's member agencies, given the contractual requirement that any charges to San Diego must be "generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2. Mr. Woodcock ignored that requirement, asserting that he "never suggested that they set rates for the 26 member agencies based on blends," and that he did not even "recall that section of the agreement saying conveyance of water." Tr. at 1938:15-1940:19 (Woodcock). But if Mr. Woodcock "never suggested" generally-applicable conveyance charges, then whatever he did suggest is irrelevant because it would violate the Exchange Agreement. *See* PTX-65 § 5.2.[20] And to the extent Met may speculate about supposedly generally-applicable

[19] *Cf. Capistrano Taxpayers Ass'n, Inc. v. City of San Juan Capistrano*, 235 Cal. App. 4th 1493 (2015) (holding that the AWWA M-1, "a mere manual," cannot "trump the plain language of the California state Constitution," and "cannot excuse utilities from ascertaining cost of service now that the voters and the Constitution have chosen cost of service").

[20] Furthermore, if Met's argument is that its own discretionary choice to provide a particular blend of SWP water somehow causes Met to incur SWP costs as conveyance costs—even though this contradicts both the Court's Phase I ruling and the evidence, and Mr. Woodcock conceded as much on cross-examination (*see* Tr. at 1933:2-1935:21)—then the same must be as true of the conveyance of blended Met water as it is for Exchange Water, and both the law and the Exchange Agreement require Met to be consistent and non-discriminatory in the way it charges for the

blend-based conveyance rates despite Mr. Woodcock's admissions, as Met's counsel seemed to suggest on redirect, *see* Tr. at 1941:25-1943:12, such rates would run afoul of the problems that led Mr. Woodcock to disclaim them in the first place. *See* Tr. at 1936:23-1941:18 (Woodcock).

For example, what would Met's blend-based conveyance rates be when Met receives very little SWP water, as has been the case recently and will only happen more if the drought continues? *See* Tr. at 1873:11-1874:10 (Woodcock). If Met's black box sends a trickle of SWP water to only one member agency, will that agency alone be "on the hook" for all of Met's fixed SWP costs, for which Met must pay even "if no water is made available"? *Id.* at 1876:11-1877:9. What happens when Met is "given a zero allocation" of SWP water? *Id.* at 1874:8. Because all member agencies would receive a zero-SWP blend in that event, and hence pay zero SWP costs on their blend-based transportation rates, Met's non-transportation rates and charges would necessarily go up because Met "must recover its costs somewhere." *Id.* at 1914:9. And once Met starts down the road of blend-based rates, it also stands to reason that the credit to which San Diego is entitled for the region-wide benefits of a full Colorado River Aqueduct (*see* Water Code § 1811(c)) should likewise fluctuate by some monthly—if not daily or hourly—measure of those benefits, which would be highest precisely when Met's SWP allocation is lowest. That, in turn, would necessitate further random increases to Met's non-transportation rates and charges during SWP shortages. But how would all of those increases be allocated? Met does not and cannot say.

Mr. Woodcock admitted that a rate structure based on blending—which Met has never considered at the administrative level, which there is no reason to believe Met's member agencies would support, for which Met provided no documentary evidence or percipient testimony at trial, and which Met never even suggests it might actually try to adopt in response to the Court's Phase I decision—"certainly would be difficult." Tr. at 1941:10-18 (Woodcock). But that was an understatement. Met's unproven, unsupported, half-baked, black-box-blend-based rate scheme would be an arbitrary and capricious mess that would violate every law underlying this Court's Phase I decision, as well as the Exchange Agreement's requirement that Met may only include

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conveyance of water, whether it is Met water or Exchange Water. *See, e.g.*, Water Code § 1813; Water Code § 109-134; PTX-65 § 5.2.

charges in the Price that are "generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies," PTX-65 § 5.2, and the statutory requirement that Met's rates must be "uniform for like classes of service throughout the district." Water Code § 109-134.[21] Thus, the Court should reject Met's damages theory, which amounts to nothing more than "putting aside the Court's opinion," Tr. at 1869:16-21 (Woodcock), in an improper effort "to use this phase to revisit the first phase." Tr. at 1880:8-9 (Court); *see, e.g.*, SOD at 53 (holding that blending is irrelevant to Met's wheeling rates).

For all of these reasons, the Court should award San Diego the damages San Diego proved it is entitled to: $188,295,602, plus interest in an amount to be addressed in subsequent briefing.

D. The Court should rule for San Diego on preferential rights.

Finally, the Court should rule for San Diego on preferential rights for the reasons the Court already articulated in denying Met's prior motion on this issue. As before, Met argues that because Met's wheeling rate and the Exchange Agreement Price include components that also factor into Met's rate for "purchase of water," the wheeling rate and the Price must also be for "purchase of water." *See, e.g.*, Met's Mar. 23, 2015 Pretrial Br. at 14-15; *cf.* Water Code § 109-135. And, as before, the "flaws in the reasoning include: (a) the components are not the same, for Price includes only some of the four items; (b) critically, the one item it does not include is the cost of water, and concomitantly (c) San Diego has already paid ***someone else*** (a third party such as Imperial) for the 'purchase of water.'" Dec. 4, 2013 Order at 7 (emphasis in original).

Met argues that the "Exchange Agreement is in substance a purchase of water at MWD's full-service rate, less the credit for water that is or in the future will be provided in kind. In other words, SDCWA is purchasing water, partly in cash and partly with a credit." Met's Pretrial Br. at 15-16. That argument fails because it contradicts the Exchange Agreement, which says nothing about San Diego purchasing water with a credit, but specifically provides that the Price is the rate "generally applicable to the ***conveyance*** of water." PTX-65 § 5.2 (emphasis added). Met's

[21] Note also that the deference inherent in the "arbitrary and capricious" standard applies only where "rate-making is a form of quasi-legislative action." SOD at 17. Mr. Woodcock's evidence-free speculations on the stand do not qualify. He is not entitled to any deference at all.

argument is also counterfactual. In practice, all wheeling transactions—including those Met itself describes as "wheeling agreements," AR2010-9656-57—are exchanges. "An exchange is the practical way [in] which all water transfers are conducted," because unless the pipeline is "completely empty," the water to be wheeled mingles with the water already in the pipeline. Tr. at 190:5-193:2 (Cushman). Thus, "all transfers are functionally executed through an exchange." *Id.* at 193:1-2. The origin and destination of specific molecules is irrelevant to the fundamental nature of the service provided, whether the contract is called a wheeling contract or an exchange agreement. Either way, the service Met provides under the Exchange Agreement, and under the agreements Met calls "wheeling agreements," is the conveyance of water, not the purchase of water. *See, e.g.*, PTX-65 § 5.2; AR2010-9656-57.

Further, Met's argument implies that it should ***at least*** give preferential-rights credit for the transactions it describes as wheeling—which are not, even under Met's interpretation, purchases of water with a "credit"—yet Met does not do so. *See* Tr. at 1083:8-12 (Cushman). The reason is clear: Met treats wheeling and exchange transactions the same, but instead of concluding, as it should, that it must therefore credit payments under both transactions to preferential rights because they are not for "purchase of water," Met concludes the opposite simply because it does not want to give preferential-rights credit for conveyance payments. Met's misinterpretation wrongly deprives those, like San Diego, who pay Met for conveyance services, but ***not*** for "purchase of water," of their statutory preferential rights. *See* Water Code § 109-135; Tr. at 988:19-989:5, 1019:13-1025:20, 1081:17-1085:12 (Cushman), 1122:14-1126:23 (Denham). The Court, therefore, should rule for San Diego on the issue of preferential rights.

V. CONCLUSION

For all of these reasons, the Court should award San Diego $188,295,602 in damages, plus interest. The Court also should issue a declaration that San Diego's payments under the Exchange Agreement, and for wheeling more generally, should count toward preferential rights. And the Court should set a schedule for further briefs and a hearing regarding interest and attorneys' fees.

Respectfully submitted,

Dated: May 22, 2015

KEKER & VAN NEST LLP

/s/ Dan Jackson

By: DAN JACKSON

Attorneys for Petitioner and Plaintiff
SAN DIEGO COUNTY WATER AUTHORITY

PROOF OF SERVICE BY ELECTRONIC TRANSMISSION

I am employed in the City and County of San Francisco, State of California in the office of a member of the bar of this court at whose direction the following service was made. I am over the age of eighteen years and not a party to the within action. My business address is Keker & Van Nest LLP, 633 Battery Street, San Francisco, CA 94111-1809.

On May 26, 2015, I served the following documents described as:

SAN DIEGO'S POST TRIAL BRIEF FOR PHASE II

by serving a true copy of the above-described documents in the following manner:

BY LEXIS NEXIS® FILE & SERVE

On the date executed below, I electronically served the documents described above via Lexis Nexis® File & Serve on the recipients designated on the Transaction Receipt located on the via Lexis Nexis® File & Serve website.

Executed on May 26, 2015, at San Francisco, California.

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Julie A. Selby