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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 MEMORANDUM IN RESPONSE TO THE COURT'S JUNE 10, 2015 ORDER FOR SUPPLEMENTAL BRIEFING

Dept.: 304

Judge: Hon. Curtis E.A. Karnow

Date Filed: June 11, 2010
June 8, 2012

Trial Date: March 30, 2015

The Court asked the parties to submit post-trial memoranda discussing (1) the applicability of sections 4.1 and 4.2 of the Exchange Agreement to the issue of preferential rights; and (2) whether any provision in the Exchange Agreement controls the issue of preferential rights in light of the statute that provides for those rights. *See* June 10, 2015 Order. San Diego respectfully submits the following response.

1. Sections 4.1 and 4.2 do not directly address preferential rights but section 4.1—the default provision—confirms that Exchange Water is *not* Met water.

San Diego's answer to the Court's first question is that sections 4.1 and 4.2 of the Exchange Agreement do not expressly address preferential rights, but they do support San Diego's argument that its payments under the Exchange Agreement should count toward its preferential rights. The fact that these contractual provisions do not mention preferential rights is part of the reason why, as the Court observed, San Diego did not discuss them in its prior briefs, focusing instead on Section 135 of the Met Act, the statute that establishes and defines preferential rights. *See id.* In fact, neither party had discussed these sections of the Exchange Agreement in the context of preferential rights until Met's Closing Brief, in which Met asserted, for the first time, that "the parties agreed that SDCWA's payments were for MWD water." Met's Closing Br. at 37:24-25. That is wrong, as San Diego demonstrated at its first opportunity, which, because there were no responsive briefs, was at the final hearing. *See* Trial Tr. at 2009:4-6.[1] San Diego appreciates the present opportunity to further refute Met's misrepresentation.

Met's belated contention that "the parties agreed that SDCWA's payments were for MWD water" is plainly false in light of section 4.1 of the Exchange Agreement, which Met never even mentions in its Closing Brief. Section 4.1 is entitled "Exchange Water as an Independent Local Supply," and provides that Exchange Water "shall be characterized ***for the purposes of all of Metropolitan's ordinances, plans, programs, rules and regulations***, including any then-effective Drought Management Plan, and for calculation of any Readiness-to-Serve Charge share, in the same manner as the ***Local Water*** of other Metropolitan member agencies, ***except as provided in***

[1] Met's decision not to raise its counter-factual interpretation of the Exchange Agreement before or during trial precluded San Diego from presenting live witness testimony to refute it.

Paragraphs 4.2 and 5.2." PTX-65 (Exchange Agr.) § 4.1 (emphases added). "Local Water" is defined in the Exchange Agreement as "water supplies not served by Metropolitan," including "water acquired" from another agency. *Id.* § 1.1(q). And no one disputes that preferential rights fall within the ambit of Met "ordinances, plans, programs, rules and regulations." So, unless it is subject to one of the exceptions, for preferential-rights consideration, Exchange Water must be treated as Local Water, not Met Water.

Section 4.2, entitled "Exception for Interim Agricultural Water Program and Determination of Price," carves out the two discrete exceptions to the default rule that Exchange Water will be treated as Local Water. It provides that "[n]otwithstanding the provisions of Paragraph 4.1, the Exchange Water delivered to SDCWA shall be characterized as Metropolitan water and not as Local Water ***only for the limited purposes*** of Paragraph 5.2 and the Interim Agricultural Water Program." *Id.* § 4.2 (emphasis added). Section 5.2 is the Price provision. *Id.* § 5.2. The Interim Agricultural Water Program no longer exists and is not relevant here.

The question, therefore, is whether preferential rights are among the "limited purposes of Paragraph 5.2." *Id.* § 4.2. The very title of section 4.2 tells us that the answer is "No." The carve-out in Paragraph 4.2 concerns the "Determination of Price," *id.*, and preferential rights have nothing to do with how Met determines the Exchange Agreement Price. Preferential rights are not mentioned in section 5.2, or anywhere else in the Exchange Agreement. Not surprisingly then, when Met's General Manager and CEO Jeff Kightlinger was asked, on direct examination, about these provisions and "how 4.2 relates to 5.2," Kightlinger's answers ***never once mentioned preferential rights***. *See* Trial Tr. at 1389:21-1391:20; 1394:11-1395:21 (Kightlinger). In fact, Kightlinger confirmed that the exception in section 4.2 was only "for the purpose of the pricing." *Id.* at 1394:23-25. If the parties had actually intended a "preferential rights exception" to the Exchange Agreement's declaration that Exchange Water shall be treated as Local Water, surely Kightlinger—and Met, prior to its post-trial briefing—would have said so.

The Parties' agreement that, for the "Determination of Price" in section 5.2, Exchange Water would be treated as Met Water rather than Local Water, has nothing to do with preferential rights. Rather, it is meant to effectuate the purpose of section 5.2: ensuring that San Diego was

charged a Price that is "generally applicable to the conveyance of water by Metropolitan on behalf of its member agencies." PTX-65 § 5.2. As the Court will recall, from the outset of the Exchange Agreement negotiations, San Diego insisted that the Price must "be non-discriminatory so that the rates would apply equally to all member agencies." PTX-58 ¶ 8; *see also* Trial Tr. at 1184:1-1185:10 (Slater); *id.* at 1646:25-1647:9 (Stapleton). That is reflected in the Price term itself, and in section 4.2, which specifies that, "for the limited purposes" of Met's Price determination, Met cannot treat Exchange Water differently from Met water. This precludes Met from doing what it, nonetheless, tried to do at trial. Met tried to elicit testimony from Jon Lambeck to the effect that Met uses cheap power to convey Met water but more expensive power to convey Exchange Water; though, in fact, he admitted that this is not what Met actually does. *See* Tr. at 1746:15-1747:10, 1765:24-1768:5, 1783:6-1790:12 (Lambeck); *see also id.* at 1724:9-20 (Court). Rightly so, because section 4.2 and section 5.2 together prohibit such discrimination.

Thus, the "limited purposes of Paragraph 5.2" are, as section 4.2 makes clear, confined to Met's Price determination. PTX-65 § 4.2. For that purpose only, Met must treat Exchange Water like its own water, in order to prevent price discrimination—*e.g.*, a higher power rate for Exchange Water than Met water. For ***all other purposes***, including preferential rights and all other "ordinances, plans, programs, rules and regulations," Exchange Water is ***not Met water***. *Id.* §§ 1.1(q), 4.1.

2. The Exchange Agreement does not control—and certainly does not waive—San Diego's preferential rights.

The Court's second question is "whether any provision in the Exchange Agreement controls the issue of preferential rights in light of the statute which provides for these rights." June 10, 2015 Order. San Diego's answer, again, is "No." As explained above, the effect of sections 4.1 and 4.2 with respect to preferential rights is to recognize Exchange Water for exactly what it is in reality: water that San Diego does not purchase from Met, but from "***someone else*** (a third party such as Imperial)." Dec. 4, 2013 Order at 7 (emphasis in original); *see also* PTX-65 §§ 1.1(q), 4.1-4.2. San Diego's preferential rights are calculated based on its total historical financial payments to Met, "excepting purchase of water." *See* West's Cal. Water Code App. §

109-135 (MWD Act § 135). Because, as the Court rightly surmised before and the language of the Exchange Agreement does not alter, San Diego is paying for the transportation of water it already purchased or developed elsewhere, San Diego's payments to Met under the Exchange Agreement should be counted toward its preferential rights.

Indeed, June Skillman, as Met's designated witness on preferential rights, admitted that "under the Exchange Agreement," San Diego "pays for the delivery of its exchange water." PTX-514 (Skillman Dep.) at 27:11-14; *id.* at 29:1-4 ("We're charging them for the delivery of their exchange water."). Met's only purported reason for treating charges that are admittedly only for the ***delivery*** of water as if they were for the ***purchase*** of water is Met's groundless fiat that "any volumetric rate that we charge" is for "purchase of water." *Id.* at 32:16-18; *see also id.* at 27:11-32:23; Met's Closing Br. at 37:12-15. That is not an interpretation of the statutory phrase "purchase of water" that might be entitled to deference. As Skillman admitted, Met's interpretation is not grounded in any sort of administrative process. *See id.* at 22:7-22. Rather, it is pure *ipse dixit,* and it makes no sense. For example, the AWWA guidelines Met purports to follow note that agencies sometimes use "volumetric charge[s]" to collect funds that are expressly ***not*** for purchase of water, but are instead used, for example, for "prefunding a major capital project," or "building necessary reserves for future requirements." 2010AR-3865 at 4056, 4058. Such charges plainly would have to be counted toward preferential rights. *See* MWD Act § 135. The same must then be true of San Diego's payments under the Exchange Agreement—as well as payments under any wheeling contracts—because those payments, as Skillman admitted, are for ***delivery***—not ***purchase***—of water.

Met apparently does contend that section 4.2 controls the issue of preferential rights.[2] The essence of Met's argument is that section 4.2 operates as a waiver of San Diego's statutory

[2] Met's arguments based on section 4.2 do not apply to what the Court, in its pre-closing argument questions, termed "pure" wheeling contracts. This is perhaps why the Court asked whether Met concedes that member agencies' payments under such contracts should count toward preferential rights. Tr. at 2037:20-2038:17. Inexplicably, Met refuses to give preferential-rights credit even for those payments, which plainly are not for the "purchase of water," because to do so, Met argues, would not "make any sense." *Id.* But the language of the statute is clear—unless it is a payment for "purchase of water," it counts toward preferential rights—and Met's attempt to elide the plain language of the statute is not entitled to deference.

preferential rights. But it cannot so operate, because waiver requires "the intentional relinquishment of a known right after knowledge of the facts." *Waller v. Truck Ins. Exch., Inc.*, 11 Cal. 4th 1, 31 (1995). "The burden is on the party claiming a waiver of a right to prove it by clear and convincing evidence that does not leave the matter to speculation, and doubtful cases will be decided against a waiver." *Id.* (citations, omissions and ellipses omitted). Here, quite obviously, San Diego did not knowingly and intentionally waive its preferential rights in connection with the Exchange Agreement. Neither section 4.2 nor any other provision in the Exchange Agreement even mentions preferential rights; and no witness testified that the treatment of preferential rights was discussed by the parties during negotiation. Thus, even if there were some ambiguity about the interaction of sections 4.1 and 4.2 with preferential rights (there is not), San Diego cannot be found to have waived its preferential rights—which San Diego's witnesses testified are critically important to its long-term planning (*see* Trial Tr. at 1020:23-1022:17 (Cushman))—by accident or inadvertence. *See Waller*, 11 Cal. 4th at 31.

Indeed, the idea that San Diego knowingly relinquished its preferential rights in the Exchange Agreement is nonsensical given that the parties executed the Exchange Agreement while the previous preferential-rights case was still pending. *See* PTX-65; *San Diego v. Met*, 117 Cal. App. 4th 13 (2004). Although the prior case involved water that San Diego undisputedly purchased from Met, not Exchange Water—which is why, as the Court already recognized, that case does not control here, *see* Dec. 4, 2013 Order at 5-7—the idea that San Diego intended to waive its preferential rights with respect to Exchange Water precisely when it was actively litigating its preferential rights with respect to Met water is untenable, and certainly is not supported by "clear and convincing evidence." *Waller*, 11 Cal. 4th at 31.

Furthermore, as June Skillman testified in her capacity as Met's person most knowledgeable about preferential rights, Met's general counsel has taken the position—which remains Met's position—that "'[b]ecause the preferential right to purchase water is a member agency right, … it is not subject to waiver by action of the Metropolitan board. Only the legislature which granted this right to the member agencies may modify or revoke it.'" PTX-514 at 53:22-55:7. Therefore, in the absence of a clear and unambiguous waiver by San Diego, Met,

cannot unilaterally effect a waiver of San Diego's preferential rights, in the Exchange Agreement or otherwise. *See Waller*, 11 Cal. 4th at 31. Notably, Met adopted this "no waivers are allowed" position in the context of deciding whether Met could adopt a drought management plan that might "revoke or modify an agency's preferential rights." PTX-514 (Skillman Dep.) at 55:9-21; *see also id.* at 37:12-38:6, 47:11-48:17, 53:19-55:7. Drought management plans are expressly included in section 4.1 as an example of Met's "ordinances, plans, programs, rules and regulations" under which it must treat Exchange Water as non-Met water. There is no reason to believe that, having expressly contracted that Exchange Water is ***not*** Met water for the purposes of drought management, San Diego silently intended the opposite for purposes of preferential rights, which are inextricably linked to drought management. *See id.*[3]

Finally, San Diego is not, as Met implied at closing argument, asking for special treatment vis à vis other Met member agencies with respect to preferential rights. San Diego's position is, and always has been, that any time a member agency contracts with Met for transportation services—whether the contract is labeled an exchange, wheeling or conveyance agreement—Section 135 of the Met Act obligates Met to provide preferential-rights credit for payments thereunder, because Met is merely conveying water that was already ***purchased*** or acquired from some other party. *See* Trial Tr. at 1083:13-1084:4 (Cushman); Dec. 3, 2014 Order at 7.[4]

For these reasons, and those set forth in San Diego's Post-Trial Brief, the Court should declare that payments for the use of Met facilities to transport non-Met water, including San Diego's payments under the Exchange Agreement, must be counted toward preferential rights.

[3] The other specific example in section 4.1 of Met "ordinances, plans, programs, rules and regulations" for which Exchange Water must be treated as non-Met water is the "calculation of any Readiness-to-Serve Charge." PTX-65 § 4.1. This example also undermines Met's argument that the "limited purposes of Paragraph 5.2" are not so limited after all, but necessarily include anything related to "payments," including preferential rights. *See* Trial Tr. at 2041:11-21. Met's RTS involves payments to Met, but does not implicate Met's Price determination. Preferential rights, just like the RTS charge, fall under the default rule that Exchange Water is Local Water, ***not*** Met water. *See* PTX-65 § 4.1.

[4] Met's suggestion that this rule somehow would require Met to give preferential rights to *non-member agencies* that pay Met for wheeling (Trial Tr. at 2038:6-9) is a red herring. Under Section 135, only Met member agencies "shall have" preferential rights. *See* MWD Act § 135.

Respectfully Submitted,

Dated: June 19, 2015

KEKER & VAN NEST LLP

By: */s/ John W. Keker*
JOHN W. KEKER

Attorneys for 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 June 19, 2015, I served the following documents described as:

SAN DIEGO'S MEMORANDUM IN RESPONSE TO THE COURT'S JUNE 10, 2015 ORDER FOR SUPPLEMENTAL BRIEFING

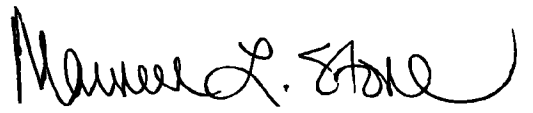
by serving a true copy of the above-described documents in the following manner:

BY FILE & SERVEXPRESS

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

Executed on June 19, 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.



Maureen L. Stone