Nos. A146901 and A148266

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA
FIRST APPELLATE DISTRICT, DIVISION THREE

---

SAN DIEGO COUNTY WATER AUTHORITY,

*Respondent and Cross-Appellant,*

v.

METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA,

*Appellant and Cross-Respondent.*

---

Appeal From Judgments And Peremptory Writs of Mandate After Court Trials
Superior Court for the County of San Francisco,
Nos. CFP-10-510830 and CFP-12-512466
The Honorable Richard A. Kramer and Curtis E.A. Karnow

---

# SAN DIEGO COUNTY WATER AUTHORITY'S RESPONDING AND OPENING BRIEF

---


KEKER & VAN NEST, LLP
JOHN W. 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
Telephone: (415) 391-5400
Facsimile: (415) 397-7188

SAN DIEGO COUNTY WATER AUTHORITY
MARK J. HATTAM – 173667
(General Counsel)
mhattam@sdcwa.org
4677 Overland Avenue
San Diego, CA 92123
Telephone: (858) 522-6791
Facsimile: (858) 522-6566

Attorneys for Respondent and Cross-Appellant
SAN DIEGO COUNTY WATER AUTHORITY

**CERTIFICATE OF INTERESTED ENTITIES OR PERSONS**
**(Cal. Rule of Court 8.208)**

San Diego County Water Authority knows of no entity or person that must be listed here under California Rule of Court 8.208(e)(1) or (2).

Respectfully submitted,

Dated: August 3, 2016

KEKER & VAN NEST, LLP

By: /s/ *Dan Jackson*
DAN JACKSON

Attorneys for Respondent and Cross-Appellant
SAN DIEGO COUNTY WATER AUTHORITY

## TABLE OF CONTENTS

**Page**

## TABLE OF AUTHORITIES

**Page(s)**

### Cases

## Constitutional Provisions



## Statutes

## Other Authorities

## INTRODUCTION

The central question here is whether Met overcharged San Diego to transport San Diego's water through Met's Colorado River Aqueduct.[1] In the parties' Exchange Agreement, Met agreed to deliver San Diego's water for no more than the costs lawfully attributable to the conveyance of water, the term of art for which is "wheeling." Instead, Met charged its System Access Rate, System Power Rate, and Water Stewardship Rate, each of which the trial court correctly invalidated as unlawful and unconstitutional.

Met's System Access Rate and System Power Rate largely consist of costs Met incurs under its contract with the State of California for a supply of water from the State Water Project ("SWP"), which has nothing to do with the transportation of water through Met's Colorado River Aqueduct or its pipeline distribution system in Southern California. Met's own administrative record proves, as the trial court found, that SWP costs are supply costs to Met, not transportation costs. And Met admitted in the resolution on which its wheeling rates are based that it includes supply costs in its wheeling rates in order to keep its supply rates low for Met

[1] Appellant and cross-respondent Metropolitan Water District of Southern California is usually referred to here as "Met," but is sometimes called "Metropolitan," "MWD," or the "District." Respondent and cross-appellant San Diego County Water Authority is usually referred to here as "San Diego," but is sometimes called "SDCWA," "SD," or the "Water Authority." Several Met member agencies filed separate notices of appeal, but they all joined Met in a single Appellants' Opening Brief ("AOB").

member agencies that do not wheel water, *i.e.*, member agencies other than San Diego. That violates the fundamental principle of "cost causation," which requires Met to charge for its services based only on what it costs Met to provide them. As Met admitted below, cost causation is the foundation for all of the legal standards at issue here, each of which independently supports the trial court's invalidation of Met's challenged rates: Article 13C of the California Constitution ("Proposition 26"); California Water Code sections 1810-1814 (the "Wheeling Statutes"); California Government Code section 54999.7(a); and the common law.

Met's Water Stewardship Rate is not a lawful "rate" under any analysis, but an unlawful tax that Met imposes on all of its member agencies to fund subsidies for Met's favored member agencies. Met does not even try to argue that its Water Stewardship Rate is based on cost causation. Moreover, Met abandoned any pretense that its Water Stewardship Rate bears a fair relationship to associated benefits when it banned San Diego from receiving such benefits in retaliation for filing this lawsuit, based on the "Rate Structure Integrity" or "RSI" clause that Met includes in all contracts for so-called "water stewardship" subsidies.

The trial court rightly held, based on detailed factual findings and overwhelming evidence, that Met's rates violate Proposition 26, the Wheeling Statutes, section 54999.7(a), and the common law. Specifically, the trial court invalidated Met's System Access Rate, System Power Rate,

Water Stewardship Rate, and wheeling rate. San Diego refers to these invalidated rates collectively as Met's "transportation rates."

The trial court further found that Met overcharged San Diego by $188,295,602 from 2011 to 2014, and owes damages in that amount under the Exchange Agreement, plus prejudgment interest in the amount of $46,637,180, for a total judgment of $234,932,782. Those findings are based on substantial evidence that San Diego introduced at trial. Met, on the other hand, refused to provide any alternative computation of damages at trial. Met first offered its alternative damages theories when it moved for a new trial, but the trial court rightly found those belated theories not only meritless, but waived. The trial court's waiver findings are "binding on this court" because they are based on substantial evidence and the trial court's "inherent power to curb abuses and promote fair process." *Peat, Marwick, Mitchell & Co. v. Superior Court*, 200 Cal. App. 3d 272, 277, 288 (1988).

Met ignores the trial court's findings and asks this Court to do the same. Yet in *California Farm Bureau Federation v. State Water Resources Control Board*, 51 Cal. 4th 421 (2011), on which Met heavily relies, the California Supreme Court held that trial courts are required to make factual findings in cases like this. *See id.* at 441-46. This Court has repeatedly held that, in "reviewing a trial court's judgment on a petition for writ of ordinary mandate, we apply the substantial evidence test to the trial court's factual findings." *Kreeft v. City of Oakland*, 68 Cal. App. 4th 46, 53

(1998); *accord, e.g., Wong v. Ohlone College*, 137 Cal. App. 4th 1379, 1382 (2006). And this is not just an ordinary mandate case; it also includes claims for breach of contract, and claims based on the Wheeling Statutes, which require factual findings about whether Met "properly included specific costs in its wheeling rate calculation or has adopted a rate that violates the statutory mandate to facilitate wheeling." *MWD v. Imperial Irrigation Dist.*, 80 Cal. App. 4th 1403, 1436 (2000). Met is wrong to ask this Court to ignore the trial court's findings about exactly those issues.

Met is also wrong to ignore dispositive cases. For example, Met never mentions *Met v. Marquardt*, 59 Cal. 2d 159 (1963), which refutes Met's argument that it has an ownership interest in the SWP. *See id.* at 200-02. And Met only includes a passing reference to *Newhall County Water District v. Castaic Lake Water Agency*, 243 Cal. App. 4th 1430 (2016), which refutes Met's argument that it is somehow immune from the requirements of Proposition 26 because it is a wholesale water supplier. The same was true of the defendant in *Newhall*, yet the court upheld the invalidation of its rates nonetheless, rejecting Met's arguments about Proposition 26 in the process. *See id*. at 1440-51. Because *Newhall* is fatal to Met's appeal, Met asked the California Supreme Court to depublish it. *See* Request for Judicial Notice (filed herewith) ("RJN"). Met's request was denied, but instead of confronting *Newhall* on appeal, Met relegates it to a dismissive footnote. *See id.*; AOB at 97-98 n.21.

As the court recently emphasized in *Hearn Pacific Corp. v. Second Generation Roofing Inc.*, 247 Cal. App. 4th 117 (2016): "There are limits to appellate advocacy, chief among them a duty of candor to the court," which "requires confronting serious potential obstacles, not burying one's head in the sand to them, be they potentially controlling adverse authorities or problematic portions of the record. . . . 'The ostrich is a noble animal, but not a proper model for an appellate advocate.'" *Id.* at 136-37 (quoting *Gonzalez-Servin v. Ford Motor Co.*, 662 F.3d 931, 934 (7th Cir. 2011) (Posner, J.)). Met's brief lacks candor and, in any event, Met's arguments fail under the law, the trial court's findings, and the substantial evidence.

Finally, San Diego cross-appealed because the trial court erred in holding that San Diego lacks standing to challenge Met's RSI clause. The trial court expressed its own doubts about that ruling, and thus went on to find that San Diego wins on the merits if it has standing, which it does, so this Court should invalidate Met's RSI clause without remand. The trial court also erred in denying San Diego its contractual attorneys' fees for the contract phase of the case. The reasonable amount of those fees was undisputed, so this Court should order Met to pay them without remand.

Thus, as shown below, the Court should affirm the judgment, the damages award, and the writ of mandate; invalidate Met's RSI clause; and order Met to pay San Diego's attorneys' fees for the contract phase.

# I. SAN DIEGO'S RESPONSE TO MET'S APPEAL

## A. STATEMENT OF THE CASE

On June 11, 2010, San Diego filed its initial action challenging the transportation rates Met adopted in April 2010 for 2011 to 2012. 1-AA-43-235. On June 8, 2012, San Diego filed a second action challenging Met's 2013-2014 transportation rates. 4-AA-981-1105. The two actions were litigated and tried together.

Specifically, San Diego challenged the validity of Met's System Access Rate, System Power Rate, Water Stewardship Rate, and the wheeling rate set forth in Met's administrative code, which includes Met's System Access Rate and Water Stewardship Rate. 4-AA-993 ¶¶ 36-37. San Diego also sought contract damages under the Exchange Agreement, which provides 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." 22-AA-6137-38 § 5.2. Met's Price under the Exchange Agreement consists of its System Access Rate, System Power Rate, and Water Stewardship Rate. 4-AA-993 ¶ 36.

San Diego also challenged Met's method for calculating San Diego's statutory right to Met water. Under section 135 of the Met Act, San Diego has a "preferential right" to Met water based on its "total payments" to Met "excepting purchase of water." Wat. Code App. § 109-135. San Diego's

payments under the Exchange Agreement, and its payments for wheeling under other contracts, are not for "purchase of water," so Met must include those payments in its calculation of San Diego's "preferential rights." But Met refuses to do so, violating section 135. 6-AA-1399-1400 ¶¶ 111-15.

**1. Relevant pretrial rulings**

The Honorable Richard A. Kramer presided over the initial stages of the litigation. On July 2, 2012, Judge Kramer overruled Met's demurrer, which was based on Met's contention that its rates were validated in perpetuity because it allegedly pledged its "rate structure" as security for its 2002 bonds. *See* 13-RT-484:24-26. Met was free to pursue that contention at trial, but chose not to, thereby waiving it—as San Diego explicitly pointed out before and after trial, without a word of dissent from Met. *See* 28-AA-7704 n.6; 33-AA-9335 n.1.

In January 2013, the Honorable Curtis E.A. Karnow took the case over from Judge Kramer. 19-RT-775:7-18. The following month, Met moved to strike Proposition 26 from San Diego's challenge to the 2011-2012 transportation rates Met adopted in April 2010, on the basis that Proposition 26, which went into effect on November 3, 2010, is not retroactive. *See* 2-RA-352-71. Met argued that "Proposition 26 eliminated the crucial presumption of validity, and imposed a new and greater evidentiary burden on local agencies. Local agencies now must prove by a preponderance of the evidence that a charge does not qualify as a tax

subject to Proposition 26 and other matters, in order to prevail." *Id.* at 368 (citing Const. art. 13C, § 1(e)). Judge Karnow agreed with Met, and thereafter applied Proposition 26 only to Met's transportation rates for 2013 and 2014 (and beyond). 7-AA-1808-31.

In July 2013—at Met's request, and over San Diego's objection—Judge Karnow bifurcated the case into two phases, the first of which would determine the validity of Met's transportation rates. *See* 2-RA-388-391. San Diego's contract claims would be decided in the second phase. *See id.* The parties later stipulated that the issue of preferential rights also would be tried in the second phase. *See* 27-AA-7454.

Judge Karnow considered hundreds of pages of briefs, cases, and other authorities on the governing standards, and then issued detailed pretrial rulings addressing each of the relevant legal theories, including:

- **Proposition 26**. Met "bears the burden of proving by a preponderance of the evidence" that its rates fall within one of seven enumerated exceptions to Proposition 26's broad definition of "tax" to mean "any levy, charge, or exaction of any kind imposed by a local government." Const. art. 13C, § 1(e). Met also must prove "that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or

benefits received from, the governmental activity." *Id.* final par. Proposition 26 requires independent review. At Met's request, however, Judge Karnow agreed to confine his independent review to Met's administrative record. *See* 7-AA-1795-97.

- **Wheeling Statutes**. The Wheeling Statutes mandate that Met "shall act in a reasonable manner consistent with the requirements of law to facilitate the voluntary sale, lease, or exchange of water and shall support its determinations by written findings." Wat. Code § 1813. The "court shall consider all relevant evidence, and the court shall give due consideration to the purposes and policies of this article," sustaining "the determination of the public agency if it finds that the determination is supported by substantial evidence." *Id.* Judge Karnow confirmed that he would do so, assigning the burden of proof to San Diego. *See* 7-AA-1798-1801.
- **Government Code § 54999.7(a)**. Section 54999.7(a) prohibits public agencies from charging other agencies more than "the reasonable cost of providing the public utility service." Gov't Code § 54999.7(a). Judge Karnow held that whether that statute applies to Met's transportation rates is a legal question he would decide independently, but that he would defer to Met on any factual issues, put the burden of proof on San Diego, and limit

his review to the administrative record, following the "general principles governing review of a quasi-legislative action on a writ of mandate under C.C.P. § 1085." 7-AA-1793, 1801-02.

- **Common Law**. Under the common law, rates are invalid if they are not based "on the cost of service or some other reasonable basis." *Cty. of Inyo v. Pub. Utilities Com.*, 26 Cal. 3d 154, 159 n.4 (1980). Judge Karnow held that, as under section 54999.7(a), he would defer to Met and follow the general rules governing judicial review of quasi-legislative decisions. 7-AA-1804-05.

**2. The Phase I Statement of Decision**

On April 24, 2014, after five days of trial, including live testimony, and after reviewing hundreds of pages of briefs and an administrative record tens of thousands of pages long, Judge Karnow issued his Phase I Statement of Decision. *See* 27-AA-7452-7517. Judge Karnow made findings of fact based on substantial evidence that he described in great detail. *See id.* He also reviewed the applicable law, concluding that under Proposition 26, the Wheeling Statutes, section 54999.7(a), and the common law, "the core inquiry is the same, and looks to cost causation, that is, whether the costs of the services (e.g. wheeling) are reasonably related to the costs of providing those services." 27-AA-7503. That was undisputed. "The parties agree that Met is obligated to set its rates based on principles of cost causation, that is, that Met must charge for its services based only

on what it costs to provide them. This is the central focus of this case" under each of "the varied causes of action." 27-AA-7498 (citations omitted). As Met put it: "Agencies that purchase Metropolitan supplied water [should] pay for supply, whereas . . . [an] agency that transports a third party's water through Metropolitan's system (known as 'wheeling') [should pay] transportation costs, but ***no supply costs***." 27-AA-7502 (emphasis added) (quoting 58-AR2012-16587).

Judge Karnow found that Met's transportation rates violate those principles for two reasons. First, Met misallocates its costs of obtaining a water supply from the SWP to its transportation rates. Second, Met's Water Stewardship Rate has no basis in cost causation, and certainly cannot be charged entirely to transportation. *See* 27-AA-7503-12.

The SWP provides a "WATER SUPPLY" for Met, as the title of Met's contract for that supply, the "SWP Contract" between Met and the State Department of Water Resources ("DWR"), expressly states. 2-AR2010-175; *see also* 27-AA-7457. "Previously, Met allocated SWP costs to supply, and none to transportation (including the SWP costs that DWR bills as its own transportation costs)." 27-AA-7504 (citing 57-AR2012-16288_1743-46; 30-RT-1676:23-1677:12). Although DWR charges Met a "transportation charge" to recover the costs of SWP "facilities whose function is the delivery of water from the sources of supply to the MWD distribution system," Met formerly allocated all of those costs to its

"Supply System" because "the function of making water available" to Met is a "supply" function for Met. 57-AR2012-16288_1744. As Judge Karnow found: "No reasonable basis appears in the record as to why this has changed." 27-AA-7504.

In fact, the administrative record proves that the reason "why this has changed," *id.*, is decidedly unreasonable. Met began to misallocate its SWP supply costs in direct response to San Diego's proposal to wheel Colorado River water from the Imperial Irrigation District ("IID"). As one of Met's earliest documents about wheeling makes clear, San Diego "raised the issue of wheeling as part of its effort to seek greater independence" from Met, but because San Diego was "the only 'likely' wheeler," Met adopted "a far different strategy" than it would have if the "political variables" had been different—*i.e.*, if member agencies other than San Diego had been likely wheelers. 62-AR2012-17126_0070, 73. Met's "strategy" was to "keep tight control of the system while assigning all system and financial risk to potential wheeling parties." *Id.* Wheeling, according to Met, "**must not negatively impact the rates or charges to any other Member Agencies.**" 27-AA-7508 (emphasis in original) (quoting 5-AR2010-1234). Met's transportation rates are still based on that protectionist position, as Judge Karnow found, and as Met's own administrative record and pleadings undeniably prove. *See id.* The express purpose and incontrovertible effect of Met's protectionism is that Met

undercharges for Met water by overcharging San Diego (and other wheelers) for the transportation of non-Met water. *See id.* That violates Proposition 26, the Wheeling Statutes, Government Code section 54999.7(a), and the common law. 27-AA-7503-09, 7515-16.

Judge Karnow also found that Met's Water Stewardship Rate is unlawful. 27-AA-7509-12. Met imposes its Water Stewardship Rate to fund subsidies "for recycling, groundwater recovery, desalinization programs and other water conservation efforts." 27-AA-7509. Assuming that it is even potentially proper for Met to impose rates to fund its so-called "water stewardship" subsidies (which it is not, as discussed below), the administrative record overwhelmingly proves that "all or at least a portion" of the costs of those subsidies must be allocated as "supply costs." 27-AA-7510 (quoting 57-AR2012-16288_2179). But Met allocates all of those costs to transportation, which is "wholly arbitrary." 27-AA-7511.

Judge Karnow concluded that Met's transportation rates are invalid "regardless of the standard" because there "is no substantial evidence in the record to support" Met's inclusion of all of its SWP costs, and all of its "water stewardship" costs, in its transportation rates. 27-AA-7516. "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." *Id.*

### 3. The Phase II Statement of Decision, the Judgment and Peremptory Writ of Mandate, and subsequent proceedings

The second trial was devoted to San Diego's claims for damages under the Exchange Agreement and declaratory relief regarding preferential rights. The trial lasted six days, including live testimony from ten witnesses. Judge Karnow again read hundreds of pages of briefs and reviewed thousands of pages of exhibits. He issued his Phase II Statement of Decision on August 28, 2015. 34-AA-9461-90.

As stated in its initial recitals, the Exchange Agreement is part of the multi-party "Quantification Settlement Agreement," or "QSA," which settled "a variety of longstanding disputes regarding the priority, use, and transfer of Colorado River water and establishes the terms for the further distribution of Colorado River water among these entities for up to seventy-five (75) years based upon the water budgets set forth therein." 22-AA-6123; *accord In re QSA Cases*, 201 Cal. App. 4th 758, 789 (2011). In the Exchange Agreement, Met agreed to deliver San Diego's Colorado River water, which San Diego acquired through two agreements that are also part of the QSA: the Transfer Agreement between San Diego and IID, under which San Diego pays IID for water IID conserves through fallowing and other extraordinary conservation measures; and the Allocation Agreement, pursuant to which San Diego obtained the rights to water conserved by

lining two earthen canals in the Imperial Valley desert, the All American and Coachella canals, with concrete. 22-AA-6123.

Judge Karnow found that Met breached section 5.2 of the Exchange Agreement. Despite Met's promise to charge only lawful conveyance rates, Met charged its unlawful System Access Rate, System Power Rate, and Water Stewardship Rate as its Price under the Exchange Agreement. 34-AA-9470. Because "Met's charges were not consistent with law and regulation, Met breached § 5.2 of the Exchange Agreement." *Id.*

Judge Karnow also found that "San Diego has offered a reasonable computation" of damages, whereas "Met did not offer a competing computation." 34-AA-9478. San Diego, therefore, proved "that it is entitled to damages in the amount of $188,295,602 plus interest." *Id.* Met failed to prove any of its affirmative defenses. 34-AA-9478-85.

Finally, Judge Karnow found that Met miscalculates San Diego's statutory right to Met water. 34-AA-9485. As mentioned above, San Diego's payments to Met, "excepting" payments for "purchase of water," must be included in Met's calculation of San Diego's "preferential right" to Met water. Wat. Code App. § 109-135. Wheeling is transportation by definition, not a "purchase of water," so wheeling payments "must be included in the preferential rights calculation." 34-AA-9487. The same is true of San Diego's payments under the Exchange Agreement: "San Diego is not purchasing water from Met. San Diego is exchanging water with Met

to make use of its own independent supplies." 34-AA-9488.

On November 18, 2015, after briefing and hearings on prejudgment interest and the form of the judgment and the peremptory writ of mandate, Judge Karnow entered final judgment for San Diego, and a peremptory writ mandating legal transportation rates. 34-AA-9582-90. The judgment invalidated Met's transportation rates for 2011 through 2014, as well as Met's methodology for calculating preferential rights, and awarded San Diego "damages in the amount of $188,295,602 on the breach of contract claims, plus prejudgment interest in the amount of $46,637,180 for a total judgment of $234,932,782.00." 34-AA-9585-86.

Met filed a motion for a new trial, asserting for the first time many of the arguments it now repeats on appeal. *See* 34-AA-9499-9502. Judge Karnow denied Met's motion, finding that Met waived its arguments by failing to assert them before, during, or even after trial, until it moved for a new trial. 34-AA-9658-66. Judge Karnow further found that, even if not waived, Met's arguments have no merit. *See id.* This appeal followed.

### B. STATEMENT OF FACTS

In its opening brief on appeal, Met ignores many dispositive facts and distorts many more. The duty of candor, however, requires an accurate statement of the facts. *See*, *e.g.*, *Hearn*, 247 Cal. App. 4th at 136-37. It is also important to provide relevant historical context. Indeed, when the validity of the Exchange Agreement was affirmed in the 2011 decision *In*

*re QSA Cases*, the court took much of its background discussion directly "from the United States Supreme Court's decision nearly 50 years ago in *Arizona v. California*," 373 U.S. 546 (1963), "[i]llustrating how deep the roots of the disputes before us go." *QSA*, 201 Cal. App. 4th at 776.

This Court need not go all the way back to the nineteenth century, as the *QSA* court did, but it is important to know that the Supreme Court in *Arizona* held that California is limited by law and agreement to a basic allotment of 4.4 million acre-feet per year ("MAFY") of Colorado River water. *See* 373 U.S. at 564-65. That was the judicial shove that set the events leading to this case in motion. *Arizona* "was particularly significant to Metropolitan and its member agencies" because, "if California was limited to receiving its basic allotment then Metropolitan would feel the brunt of the shortfall," leaving Met's Colorado River Aqueduct "over half empty." *QSA*, 201 Cal. App. 4th at 785; *see also* 41-RT-2647:26-2651:1 (Kightlinger). *Arizona* hit Met harder than IID because IID's entitlement to Colorado River water is higher in priority, meaning that IID can "divert its full right to water before Metropolitan can divert any water at all." *Cty. of Imperial v. Superior Court*, 152 Cal. App. 4th 13, 19 (2007); *see also* 1-RA-232; 29-RT-1393:10-18 (Cushman). It took California's many interested parties forty years—from 1963, when *Arizona* was decided, to 2003, when the agreements comprising the QSA, including the Exchange Agreement, were executed—to put together a plan to comply with *Arizona*.

In fact, as Marc Reisner reported in his "brilliant—if opinionated—classic *Cadillac Desert*,"[2] California Governor Edmund Gerald "Pat" Brown, Sr. saw the writing on the wall even before *Arizona* was decided, and proposed the SWP as a solution to California's impending shortage of Colorado River water. MARC REISNER, CADILLAC DESERT: THE AMERICAN WEST AND ITS DISAPPEARING WATER 347-55 (2d ed. 1993). Met, on the other hand, originally opposed the SWP because Met was arguing—to the Supreme Court, to the newspapers, to anyone who would listen—that California needed every drop it was taking from the Colorado River, and that Arizona should not be allowed to build its Central Arizona Project. *Id.* at 349. If California built its own water project, that would "wash away the strategic foundation" of Met's "legal and moral argument. It was an absurd position to be in," but "Met was committed—it had to pretend that no water was available from anywhere else." *Id.* So "Met went after the idea hammer and tongs, arguing against it on every conceivable ground: cost, need, feasibility, practicality, even morality," but Pat Brown was confident that "Met would be brought into the fold." *Id.* at 350. Sure enough, on November 4, 1960—just four days before the voter referendum on the SWP—Met "capitulated" by signing the SWP Contract. *Id.* at 354; *see also Marquardt*, 59 Cal. 2d at 202.

---

[22] *Capistrano Taxpayers Ass'n, Inc. v. City of San Juan Capistrano*, 235 Cal. App. 4th 1493, 1497 (2015) (Bedsworth, J.).

The SWP and Met's Colorado River Aqueduct are shown in the map below, 6-RA-1525, which Met created:


In the legend of its map, Met correctly identifies the California Aqueduct, which is part of the SWP, as a "STATE AQUEDUCT." *See* 28-RT-1369:7-1372:4 (Cushman). Met has admitted, and it is factually and legally indisputable, that the State, not Met, owns and operates the SWP. 9-AA-2330-2332, Admissions 44-47; 28-RT-1291:2-4; *Marquardt*, 59 Cal. 2d at 200-02. Met, on the other hand, owns the Colorado River Aqueduct, which is accurately labeled a "LOCAL AQUEDUCT." 6-RA-1525.

### 1. Met's SWP Contract and the *Marquardt* case

Met's SWP Contract was validated by the California Supreme Court

in *Marquardt*—which, like *Arizona*, goes unmentioned in Met's brief, yet is essential for understanding this case. In an echo of Met's original opposition to the SWP, *Marquardt* was technically a lawsuit between Met and its own Executive Secretary, James Marquardt, who allegedly refused to carry out the SWP Contract "based on his assertion that the contract is invalid." 59 Cal. 2d at 170. But that was just a legal fiction enabling Met to fulfill its contractual obligation to seek judicial validation of the SWP Contract. *See 2*-AR2010-189 art. 3.

One of the questions in *Marquardt* was whether the SWP Contract caused Met to exceed its statutory limit on indebtedness. 59 Cal. 2d at 200. "That limit could be exceeded only if the district's 'indebtedness' were viewed as being the aggregate amount of all payments to be made throughout the entire term of the contract. Such a view would be unsound," as the California Supreme Court explained:

> Although the contract, insofar as it provides for the contractors to return to the state all costs of the project, ***has a slight resemblance to an agreement for the purchase of an interest in a water system*** on the installment plan, ***it has a much greater resemblance to a contract for the furnishing of continued water service in the future***. All payments to be made by the district are contingent on future performance of contractual duties by the state. (Art. 29.) ***The district does not obtain ownership of any facilities, ownership by the state being expressly provided for***. (Art. 17(f)(1), 17(f)(2).) ***Nothing in the contract indicates that the state shall hold title as a trustee or that the district shall be an equitable owner***. To consider this contract as a purchase on the installment plan and all future payments under it as a single indebtedness incurred at the outset would be unrealistic.

*Id.* at 201-02 (emphases added).

So much for Met's assertion that it has an ownership interest in the SWP because the SWP Contract "is not a typical purchase or supply contract." AOB at 63. The California Supreme Court held the opposite in *Marquardt*. Met must pay its bills to ensure "continued water service," 59 Cal. 2d at 201, but does not "own the cost" of the SWP, as Met erroneously contends on appeal. AOB at 102. On the contrary, the "State shall be and remain the owner of such project transportation facilities or portions thereof constructed in whole or in part with funds provided by the District." 2-AR2010-216, art. 17(f)(1). Met does not acquire any ownership interest in those "transportation facilities," *id.*, only a "WATER SUPPLY," as the SWP Contract makes clear. 2-AR2010-175.

As Judge Karnow found, Met originally recognized that its payments under the SWP Contract—specifically including the payments DWR invoices as "transportation" charges—are supply costs to Met. 27-AA-7504 (citing 57-AR2012-16288_1743-46; 30-RT-1676:23-1677:12). Indeed, Met's counsel conceded at trial that "it is true" that Met's experts considered this issue back in 1969, and put SWP charges, including DWR's "transportation" charges, "***all into supply***." 30-RT-1676:12-1677:12 (emphasis added). Likewise:

- Met's experts at Resource Management International ("RMI") allocated all of Met's SWP costs to the "Supply Function." 4-

AR2010-1104, 1112. SWP costs are "Supply Costs," and "are not incurred to provide wheeling service." 5-AR2010-1234, 1249.

- Another of Met's experts, George A. Raftelis, explained in his textbook that "water right purchases" are "*supply*" costs. 57-AR2012-16288_5291 (emphasis in original).
- The accounting standards of the National Association of Regulatory Utility Commissioners ("NARUC") dictate that the category for supply costs "shall include the cost at the point of delivery of water purchased for resale." 57-AR2012-16288_1757. As the California Public Utilities Commission has explained, that "includes charges for readiness to serve and . . . payments for the right to divert water at the source of supply." 1-RA-60.
- San Diego's experts further explained that, because Met admittedly "does **not** own or operate, maintain, or operate any of the SWP facilities, the SWP costs are a MET cost of Supply and not a cost of Conveyance and Aqueduct service." 39-AR2010-11208 (emphasis in original). The "other SWP contracting agencies" recognize this and "allocate SWP costs as supply costs." 39-AR2010-11209; *see also* 40-AR2010-11393-400; 57-AR2012-16215-16. DWR "breaks out its own 'supply' and 'transportation' costs in invoices," but that does not mean that DWR's transportation costs are transportation costs for purposes of ***Met's*** cost allocations; on the contrary, ***all*** SWP costs are supply costs for Met. 57-AR2012-16161.

### 2. Met's 1997 wheeling rate and the *MWD* case

Although *Arizona* limited California's allotment of Colorado River water to 4.4 MAFY in 1963, "California was nonetheless able to use much more than that because Arizona and Nevada were not yet able to use their full entitlements." *QSA*, 201 Cal. App. 4th at 773. By 1986, however, the construction of the Central Arizona Project was well under way, and California's "single most pressing water problem" was "how to replace the Southern California Metropolitan Water District's former Colorado River supplies now that Arizona has begun to claim its full share." 5-RA-1216. One solution would be for San Diego to "purchase conserved waters" from IID, 5-RA-1258, but San Diego would need to wheel that water through Met's Colorado River Aqueduct, which was San Diego's express reason (in addition to public policy) for supporting the Wheeling Statutes, which were enacted in 1986. *See id.*; Wat. Code §§ 1810-1814.

From 1987 to 1992, California suffered a drought that was particularly hard on San Diego. Because of Met water shortages, San Diego lost roughly a third of its water supply for more than a year. 28-RT-1378:7-25 (Cushman). In desperate need of more reliable sources of water supply, San Diego negotiated its Transfer Agreement with IID. *See id.*; 21-AA-5882-5992. It was clear that Met would have plenty of capacity to wheel that water because the *Arizona* decision, once enforced, would leave the Colorado River Aqueduct "over half empty." *QSA*, 201 Cal. App. 4th

at 785; *see also* 41-RT-2620:7-10 (Slater), 41-RT-2647:26-2651:1 (Kightlinger).

As already discussed, Met's response to San Diego's negotiations with IID was to take the position that wheeling "**must not negatively impact the rates or charges to any other Member Agencies**." 27-AA-7508 (emphasis in original) (quoting 5-AR2010-1234). From the outset, Met's experts warned that "it is virtually unthinkable that there is any remotely acceptable wheeling rate that could in fact be imposed that would hold MWD and the other agencies harmless"—*i.e.*, "avoid any rate escalation for 'non-wheeling' member agencies." 62-AR2012-17126_0078. San Diego agreed, unsurprisingly, but so did experts hired by Los Angeles and the Municipal Water District of Orange County, two of Met's largest member agencies; as did Met's own Assistant Chief of Planning and Resources, Brian Thomas, who later became Met's Chief Financial Officer. *See* 7-AR2010-1750, 1757; 62-AR2012-17126_0111. Likewise, Met's experts at RMI explained the many problems Met would create by setting rates based on protectionism instead of cost causation:

> The rate could be perceived as excessive. Member Agencies will likely argue that the rate includes costs not incurred to provide wheeling service (e.g., fixed SWP costs, CRA fixed and variable costs, fixed O&M). . . . Water marketers may argue that the rate will distort the market for water transfers and discourage the transfer of water from low value to high value uses. . . . The rate could be criticized as an obstacle to efforts to easing water shortages by water transfers if Metropolitan is unable to make full deliveries to Member

> Agencies. . . . In addition, [it] could be considered well in excess of the costs of providing within-system wheeling. Member Agencies could argue that all supply related costs should be removed from the within-system wheeling rate. . . . Could discourage transactions that would be economical at a lower wheeling rate and lead to criticism that Metropolitan is impeding efforts to alleviate shortages through in-basin transfers . . . [and] will artificially depress the market price of water and impede formation of a robust water market.

5-AR2010-1249-50.

RMI further explained that Met could avoid all of those problems, as well as the potential problem of revenue losses from wheeling, if it would "formally allocate its supply entitlements among Member Agencies on a long-term basis." 5-AR2010-1254_01 n.18. That and other approaches based on cost causation "could substantially lessen the potential for revenue losses due to the displacement of Metropolitan's sales by the wheeling of third-party water." 5-AR2010-1254. By securing commitments from member agencies to pay SWP costs, Met "would increase the certainty of revenue recovery over the long-term." 5-AR2010-1254_01 n.18.

Nevertheless, on January 14, 1997, Met adopted Resolution 8520, which Met continues to cite as the "written findings" required by the Wheeling Statutes for Met's 2011-2014 wheeling rates. *See* Wat. Code § 1813; 26-AA-7157:3-7158:14. Resolution 8520 begins with a series of "WHEREAS" clauses, in which Met declares that the SWP is part of Met's own "conveyance system," and that the Wheeling Statutes prohibit "financial injury" to non-wheelers. 9-AR2010-2446-47. Met goes on to

"find" that Met's conveyance system includes its "rights in the State Water Project system." 9-AR2010-2449 § 5. Met "finds" that it is "necessary" to include "unavoidable costs attributable to Metropolitan's supply," including SWP costs, in its wheeling rate "in order to protect Metropolitan's member agencies from financial injury by avoiding the shifting of those costs from a wheeling party to Metropolitan's other member agencies." *Id.* § 7. And Met "finds" that including supply costs in its wheeling rate is "reasonable and consistent with all applicable requirements of law, including any requirement to facilitate the voluntary sale, lease or exchange of water, while ensuring that the use of Metropolitan's conveyance system is fairly compensated and does not injure any other legal user of Metropolitan's water and conveyance system." 9-AR2010-2450 § 13.

After adopting Resolution 8520, Met sued to validate its wheeling rate. The trial court ruled against Met as a matter of law, without deciding factual questions such as whether Met "properly included specific costs in its wheeling rate calculation or has adopted a rate that violates the statutory mandate to facilitate wheeling." *MWD*, 80 Cal. App. 4th at 1436. Division 5 of the Second District held that the trial court erred by invalidating Met's wheeling rate solely "*as a matter of law*," under "any and all circumstances," and remanded for a trial "in compliance with section 1813." *Id.* at 1427-28, 1436 (court's emphasis). But Met decided not to go to trial after all because, less than a month after Division 5's remand,

Division 6 explicitly rejected Resolution 8520's premise that the Wheeling Statutes prohibit what Met mistakenly refers to as "injury" from higher supply rates. *See San Luis Coastal Unified Sch. Dist. v. City of Morro Bay*, 81 Cal. App. 4th 1044, 1050 (2000); *cf.* 9-AR2010-2447-50.

Rather than proceed to trial under *Morro Bay*, Met dismissed the *MWD* case and "unbundled" its postage-stamp water rate into a number of individual rates "to reflect the different services provided by Metropolitan." 21-AR2010-5708. Met's "unbundled" rates included its Supply Rate, System Access Rate, System Power Rate, Water Stewardship Rate, and a wheeling rate consisting of the System Access Rate, the Water Stewardship Rate, and other charges. 21-AR2010-5707-16. As San Diego noted at the time, "although a new series of 'labels' is created for various rate-setting concepts," the underlying reality is Met's continued "refusal to allow fair access to the conveyance and distribution system that serves Southern California." 18-AR2010-4764. Met's documents about its "unbundled" rates prove that its strategy was still to overcharge for transportation, in order to undercharge for supply, in order to be more "competitive with a supplier that does not have to pay these costs." 1-RA-201.

### 3. The 1998 Exchange Agreement

Meanwhile, in October 1997—while the *MWD* case was still pending—the Legislature passed an emergency bill directing the DWR Director, David Kennedy, to help Met and San Diego negotiate a fair

wheeling rate for San Diego's water from IID, and if they could not agree to one, to "issue a formal recommendation." 1997 Cal. Legis. Serv. Ch. 874, S.B. 1082 (Oct. 12, 1997) ("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" of the Wheeling Statutes, including the wheeling rate. *Id.* Director Kennedy was "extremely well-regarded" by everyone involved, including the Governor, the Legislature, San Diego, and Met. 41-RT-2552:16-2556:8 (Slater). The Legislature took the unusual step of empowering him to determine the wheeling rate 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.

At the time, Met's rate for wheeling "as space is available" was $141/AF "plus the cost of power necessary to move the water." 1-RA-114. Met offered to cut that in half for the IID transfer based on its regional benefits, after initially trying to conceal Met's own calculations of those benefits. *See* 1-RA-115; 1-RA-95. But that purportedly "discounted" rate was still far too high. In fact, Met's internal calculations showed that its actual costs of wheeling were only "about $10/AF plus energy costs." 62-AR2012-17126_109. In other words, Met's general rate for wheeling on a "space available" basis was fourteen times higher than Met's actual costs,

and its so-called "discount" rate for "space available" wheeling was seven times higher than its actual costs. *See id.*; 1-RA-115.

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," taking "into account Metropolitan's fixed system costs and the regional benefits provided by San Diego bringing conserved IID water to the region," as required under the Wheeling Statutes. 32-AA-9113 n.4; *see also* Wat. Code § 1811(c). Met "would have had to do a comparable IID conservation/transfer agreement as a component of the 4.4 Plan" to keep California within *Arizona*'s limits, but "by SD arranging for this block of water to meet its needs, MWD does not have to develop this amount of new supply in its overall water supply program." 32-AA-9113 n.3.

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." 41-RT-2553:6-2556:8 (Slater). Accordingly, on January 13, 1998, Met's Board directed its negotiators to proceed "within the framework proposed by Director David Kennedy." 11-AR2010-2972 at 2977. On April 29, 1998, San Diego and IID executed their Transfer Agreement 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* 11-AA-2929-2930 § 7.1(e). On November 10, 1998, San Diego and Met executed the 1998 Exchange Agreement. 1-RA-129-180. The price term was based on Director Kennedy's $80/AF wheeling rate, and expressly excluded "any costs of the State Water Project." *Id.* § 5.4.

At first, Met lauded the "potentially historic agreement" as "the culmination of an almost three year process to determine the major components of a transaction to move the water from IID to SDCWA," which "came about with the involvement of many in the water community, the state legislature, and the governor's office." 1-RA-123. As Met's Brian Thomas emphasized, the "transaction, if completed, will have benefits for the state, Metropolitan's member agencies, and San Diego":

> a. The **state** benefits because this is one piece of the larger California 4.4 Plan that will ensure that Metropolitan's Colorado River Aqueduct is full, thus reducing pressure on the Bay-Delta. Stabilizing supplies on the Colorado River benefits not only Metropolitan, but Coachella and IID, as well.
>
> b. **Metropolitan's member agencies** benefit from a full Colorado River Aqueduct, the additional supplies of surplus water at near zero cost, and the resolution of longstanding disputes regarding Colorado River supplies.
>
> c. San Diego benefits by acquiring an independent supply of water, meeting one of their stated goals.

*Id.* (emphases in original).

But then, like Pharaoh, Met hardened its heart and refused to let the water go. Met went to court to object that IID could not transfer any water

to San Diego after all because Met claimed entitlement to any water IID did not use—although Met later abandoned that claim in exchange for 100,000 AFY of the conserved water. *Imperial*, 152 Cal. App. 4th at 20-22. Met also gathered "opposition research on public officials and others involved with the water transfer," which "incensed lawmakers," who responded by enacting a special law requiring Met to "establish and operate an Office of Ethics." Cal. B. An., S.B. 60 (Apr. 7, 1999); Wat. Code App. § 109-126.7. And Met asserted that a condition precedent to the 1998 Exchange Agreement was unsatisfied, and might never be satisfied, because Met had not yet received funding from the State to line the All American and Coachella canals. *See* 1-RA-152 § 8.1(d); 41-RT-2549:8-2551:24 (Slater), 42-RT-2864:16-2865:20 (Stapleton). For these and other reasons, Met never delivered any water under the 1998 Exchange Agreement.

**4. The 2003 Amended and Restated Exchange Agreement**

In 2003, the Secretary of the Interior finally implemented the *Arizona* Court's 4.4-MAFY restriction on California's share of Colorado River water. Met went "from a full aqueduct in 2002 to roughly a half aqueduct in 2003," losing "about 5-, 600,000 acre-feet of water overnight." 41-RT-2650:7-22 (Kightlinger). This redoubled the pressure for the transfer water to finally begin flowing, so the parties agreed to renegotiate, amend, and restate their Exchange Agreement. *See id.*; 22-AA-6122-56.

Met "believed that the true cost of conveying the water to San Diego

was somewhere around $250 an acre-foot," whereas "San Diego's view was it was somewhere around $80, $90 an acre-foot"—the amount Director Kennedy had found to be fair. 41-RT-2658:12-15 (Kightlinger); *see also* 32-AA-9110-13. Unable to resolve that dispute, the parties agreed to a five-year peace treaty. *See* 1-RA-220 ¶ 8. San Diego would pay Met's inflated wheeling rate for five years, and then sue to obtain a lawful wheeling rate if the parties' dispute about Met's wheeling rate was still unresolved. *See id.*; 40-RT-2399:24-2400:15, 2406:5-2408:12 (Cushman); 2557:12-2580:8 (Slater); 42-RT-2859:13-2870:24, 43-RT-2886:15-2894:6, 2894:192898:16 (Stapleton).

The parties also agreed that the term of the amended Exchange Agreement would match that of the Transfer Agreement. That solved a problem with the 1998 Exchange Agreement, which would have expired with fifteen years still remaining on the Transfer Agreement, at which point San Diego would be paying to conserve 3 million acre-feet of IID water with no commitment from Met to deliver it at any price. *See* 40-RT-2412:2-21, 2464:24-2465:6 (Cushman), 41-RT-2546:17-2548:11 (Slater), 42-RT-2864:16-2865:20 (Stapleton), 41-RT-2657:15-2658:15 (Kightlinger); 6-RA-1526. In the amended Exchange Agreement, San Diego was "trading 15 years of complete uncertainty . . . for five years of paying whatever rate Metropolitan asked." 40-RT-2464:24-2465:6 (Cushman).

Given Met's stated "insecurity over funding and other issues related to implementing the canal lining," San Diego also agreed to "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." 41-RT-2551:25-2552:15 (Slater). San Diego took "considerable risk in carrying out the project," including the 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 come through with the money and, if it did, whether it would be enough. 40-RT-2465:7-2466:4 (Cushman). "Nobody wrote the Water Authority a check for $235 million at the time." *Id.* at 2465:12-13.

San Diego also knew that it would need to join forces with Met to defend the QSA, which was the historic outcome of an "unprecedented campaign" 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. 40-RT-2575:9-18 (Slater); *see also QSA*, 201 Cal. App. 4th at 772-95. Met had previously tried to hijack or sabotage those negotiations. *See, e.g.*, *Imperial*, 152 Cal. App. 4th at 20-21; Cal. B. An., S.B. 60 (Apr. 7, 1999). Not only San Diego, but all of California needed Met to finally stop obstructing the transfer and start helping to defend the QSA, including the Exchange

Agreement, in the litigation that "immediately ensued." 41-RT-2575:9-2576:2 (Slater); *see also QSA*, 201 Cal. App. 4th at 772-95, 838-42.

The parties executed the amended Exchange Agreement on October 10, 2003, at a "signing event" for "all 30-some agreements" that comprise the QSA. 41-RT-2667:23-2668:1 (Kightlinger). The crucial section of the Exchange Agreement for present purposes is 5.2, which provides 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." 22-AA-6137-38 § 5.2. After the five-year peace treaty, "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." *Id.*

**5. Met's 2011-2014 transportation rates and Met's retaliation against San Diego for challenging those rates in this case**

Met adopted its rates for 2011 and 2012 in April 2010, and adopted its rates for 2013 and 2014 two years later—all over San Diego's longstanding objections. *See* 39-AR2010-11203-214; 40-AR2010-11343-92; 40-AR-2010-11564-574; 57-AR2012-16154-16241; 60-AR2012-16995-17013; 62-AR2012-17098-126. Met purported to justify its inclusion of its SWP supply costs in its transportation rates by putting an allegedly "independent" analysis by Mr. Raftelis into the administrative

record. 40-AR2010-11309. But the crucial opinion in that analysis was suborned by Met's budget manager, June Skillman, and Met's assistant general counsel, Sydney Bennion. *See* 1-RA-278-79. Ms. Skillman admitted that Mr. Raftelis did not write that purportedly "independent" opinion; ***Ms. Skillman wrote it with this litigation in mind***. 31-RT-1920:21-1921:1, 1926:20-1931:1, 1935:2-9.

Met did not even attempt to justify charging its Water Stewardship Rate as a transportation rate. On the contrary, Met admits that it made no effort to evaluate its Water Stewardship Rate based on the principles of cost causation. *See* 9-AA-2316-2325, Admissions 17-43. Met also admits that it made no effort to ensure that its "water stewardship" costs are apportioned fairly. *See id.* In fact, Met ensured the opposite.

In June 2004, Ronald Gastelum, then Met's Chief Executive Officer, and Jeffrey Kightlinger, who was then Met's General Counsel, and later became its CEO, created Met's RSI clause in direct response to San Diego's reservation of its "right to challenge Metropolitan's uniform wheeling rates after five years." 28-AR2010-7823-26; *see also, e.g.*, 42-RT-2726:25-2735:21 (Kightlinger); 1-RA-267-271; 1-RA-272-275; 1-RA-266. Met's RSI clause was designed to prevent and punish "litigation challenging Metropolitan's rate structure." 1-RA-284. If a member agency dares to challenge the legality of Met's rates, Met terminates subsidies to that agency for local water conservation and water supply development

programs, which Met funds through its Water Stewardship Rate. *See* 29-RT-1401:1-1402:12, 1407:9-1412:4, 40-RT-2412:27-2415:21 (Cushman); 31-RT-1845:23-1850:4 (Upadhyay); 42-RT-2726:25-2735:21 (Kightlinger).

After San Diego filed this lawsuit, Met retaliated—as planned—by invoking its RSI clause to terminate most of San Diego's existing subsidies and ban San Diego from receiving future subsidies. *See* 1-RA-286-295; 1-RA-284-285; 29-RT-1407:9-1412:4, 40-RT-2415:22-2416:19 (Cushman); 31-RT-1845:23-1850:4, 42-RT-2771:27-2773:28 (Upadhyay). But Met still imposes its Water Stewardship Rate on San Diego. 29-RT-1411:22-24, 1014:12-19 (Cushman). From 2011 to 2014, San Diego paid roughly $77 million in Water Stewardship Rate charges, but only received approximately $22 million from the few legacy subsidies Met had not terminated. 40-RT-2416:28-2419:4 (Cushman).

In sum, Met has overcharged, and continues to overcharge, San Diego by hundreds of millions of dollars to deliver Colorado River water that is vital not only to San Diego, but to Met, its other member agencies, and the rest of California, but which Met would rather let evaporate in the desert than deliver to San Diego for a fair and lawful price.

## C. ARGUMENT

### 1. Judge Karnow correctly found, based on substantial evidence, that Met's transportation rates violate Proposition 26.

#### a. Standard of Review

Although Met generally—and incorrectly—contends that the Court should decide this appeal "without reference to the superior court's findings," AOB at 53,[3] Met admits that, under Proposition 26, this Court must review those findings "under the substantial evidence standard," which Met describes as "highly deferential." *Id.* at 56, 88. This Court's review is "de novo to the extent that the court decided questions of law concerning the construction of constitutional provisions and not turning on any disputed facts." *Schmeer v. Cty. of Los Angeles*, 213 Cal. App. 4th 1310, 1316 (2013). But, to the extent Judge Karnow's decisions turned on disputed facts—as they generally did—this Court reviews them under the "substantial evidence standard." *Id.* And, to the extent Judge Karnow's findings turned on credibility, they cannot be second-guessed. *Lauderdale*

[3] The cases Met cites for this proposition do not support it. *Western States Petroleum Ass'n v. Superior Court*, 9 Cal. 4th 559 (1995), was about the admissibility of evidence, not the standard of review; and *Friends of the Old Trees v. Department of Forestry & Fire Protection*, 52 Cal. App. 4th 1383 (1997), was an "administrative mandamus" case under Code of Civil Procedure section 1094.5. *Id.* at 1387. As Met itself has argued throughout this litigation, including to this Court, such cases are "inapposite" here because this is not an administrative mandamus case under section 1094.5. *See* 2-RA-316-317; 2-RA-345. On the contrary, this is an ordinary mandamus case under section 1085, as well as a contract case and one asserting violations of the Wheeling Statutes, all of which required Judge Karnow to make factual findings based on substantial evidence, as he did.

*Assocs. v. Dep't of Health Servs.*, 67 Cal. App. 4th 117, 125 (1998).

Met appears to be suggesting that Judge Karnow should not have made factual findings at all, but that suggestion plainly contradicts the California Supreme Court's decision in *Farm Bureau*, on which Met elsewhere relies heavily. *See* AOB at 82, 88, 90, 96-97, 99. The "province of the trial court" is "to decide questions of fact," whereas appellate courts "decide questions of law." *Farm Bureau*, 51 Cal. 4th at 442 (quoting *In re Zeth S.*, 31 Cal. 4th 396, 405 (2003)). Accordingly, the trial court in *Farm Bureau* was explicitly "directed to make detailed findings" on issues remarkably similar to those on which Judge Karnow made his findings, including whether the costs at issue "were reasonably related to the fees assessed on the payors" and "reasonable" in amount; "whether the statutory scheme and its implementing regulations provide a fair, reasonable, and substantially proportionate assessment of all costs"; and whether the costs of the Central Valley Project—the "FEDERAL AQUEDUCT" shown on the map above, 6-RA-1525—were allocated fairly based on the "beneficial interest" of those charged. 51 Cal. 4th at 428, 442-46. The concurrence further emphasized the need for factual findings given the defendant's reliance on an apparently litigation-inspired document of "uncertain reliability." *Id.* at 447-48 (Moreno and Werdegar, JJ., concurring).

Met's argument also contradicts *MWD*, another case on which Met relies heavily but mistakenly. *See* AOB at 31, 56, 62, 72-74, 82-83, 86.

*MWD* was remanded precisely because the trial court invalidated Met's wheeling rate solely "*as a matter of law*," rather than as a matter of evidence and public policy "as provided for in section 1813." *MWD*, 80 Cal. App. 4th at 1422, 1427 (court's emphasis). If Met had not dismissed that case, the trial court would have decided whether Met "properly included specific costs in its wheeling rate calculation or has adopted a rate that violates the statutory mandate to facilitate wheeling," *id.* at 1436, which is precisely what Judge Karnow decided here. 27-AA-7503-09. Met seems to concede, albeit without thinking it through, that in doing so, Judge Karnow made factual findings. *See* AOB at 56 n.15. This Court reviews those findings under the deferential "substantial evidence test." *Kreeft*, 68 Cal. App. 4th at 53; *see also* AOB at 56-57. Met, on the other hand, did not make any factual findings in adopting its wheeling rates, but instead continues to rely on the erroneous conclusions in its Resolution 8520. *See* 26-AA-7157:3-7158:14; 9-AR2010-2446-51. "This conclusory resolution, which does not contain any evidence or factual information, does not constitute substantial evidence." *City of Livermore v. Local Agency Formation Com.*, 184 Cal. App. 3d 531, 542 (1986).

Realizing that it has no substantial evidence to support its transportation rates, Met argues that those rates can only be invalidated if they are "arbitrary and capricious," relying on *Brydon v. East Bay Municipal Utility District*, 24 Cal. App. 4th 178 (1994). *See* AOB at 54.

But *Brydon* was overturned by Proposition 26, and before that Proposition 218, both of which were designed to place "stricter controls on local government discretion." *Newhall*, 243 Cal. App. 4th at 1451 n.6 (quoting *Capistrano*, 235 Cal. App. 4th at 1512-13). Indeed, Met convinced Judge Karnow not to apply Proposition 26 retroactively precisely because "Proposition 26 eliminated the crucial presumption of validity, and imposed a new and greater evidentiary burden on local agencies. Local agencies now must prove by a preponderance of the evidence that a charge does not qualify as a tax subject to Proposition 26 and other matters, in order to prevail." 2-RA-368 (citing Const. art. 13C, § 1(e)). Met is judicially estopped from arguing otherwise now. *See Jackson v. Cty. of Los Angeles*, 60 Cal. App. 4th 171, 183 (1997).

In any case, the law is clear that the series of voter initiatives that culminated in Proposition 26 eliminated the deference that Met heavily relied upon in decades past, and wrongly insists upon even now. *See*, *e.g.*, *Silicon Valley Taxpayers Ass'n v. Santa Clara County Open Space Authority*, 44 Cal. 4th 431, 443-50 (2008). Contrary to Met's arguments on appeal, the doctrine of separation of powers does not and cannot support Met's demands for deference in the face of the voters' decision to eliminate such deference. The requirements of Proposition 26, like those of Proposition 218, "are contained in constitutional provisions of dignity at least equal to the constitutional separation of powers provision." *Id.* at 448.

In short, Judge Karnow is entitled to the deference that Met wrongly claims for itself. *See* AOB at 56-57, 88.

**b. *Newhall*, among other cases, confirms that Met's transportation rates violate Proposition 26.**

*Newhall*, which was decided nearly two years after Judge Karnow's Phase I decision, confirms that Judge Karnow correctly invalidated Met's transportation rates under Proposition 26. As already mentioned, Met asked the California Supreme Court to depublish *Newhall*, but Met's depublication request was denied. *See* RJN. Nevertheless, Met pretends that *Newhall* is not the law, violating its duty of candor to this Court. *See* AOB at 97-98 n.21; *Hearn*, 247 Cal. App. 4th at 136-37.

The defendant in *Newhall* (the "Agency"), just like Met, was a "wholesale water agency" selling "imported water, purchased primarily from the State Water Project." 243 Cal. App. 4th at 1434. The plaintiff challenged a component of the Agency's rates that was "based on each retailer's three-year rolling average of total water demand (that is, its demand for the Agency's imported water *and* for groundwater not supplied by the Agency)." *Id*. at 1438 (court's emphasis). The Agency purported to justify that rate component on the grounds that "there is a direct nexus between groundwater availability and imported water use," and "since all retail purveyors benefit from imported water and the Agency's activities, they should pay for the reasonable fixed costs of the system in proportion to

the demand (i.e. burdens) they put on the total water supply regardless of how they utilize individual sources of supply." *Id.* at 1438-39. The trial court rejected that rationale and awarded the plaintiff a refund. *Id.* at 1440.

The Court of Appeal affirmed, holding that the Agency's rates violated Proposition 26 for two reasons. "First, the rates violate Proposition 26 because the method of allocation does not 'bear a fair or reasonable relationship to the payor's burdens on, or benefits received from,' the Agency's activity." *Id.* at 1441 (quoting Const. art. 13C, § 1(e), final par.). The court referred to that as the "proportionality requirement." *Id.* Second, the purported benefit was "at best indirect," so the rates did not qualify for Proposition 26's exception for rates "imposed 'for a specific government service or product provided *directly* to the payor that is *not* provided to those not charged.'" *Id.* at 1441, 1451 (court's emphases) (quoting Const. art. 13C, § 1(e)(2)).

The *Newhall* court rejected the argument—which Met nevertheless repeats here—that "the proportionality requirement is measured 'collectively,' not by the burdens on or benefits received by the individual purveyor." 243 Cal. App. 4th at 1442; *cf.* AOB at 96-100. The cases cited for that proposition—*Griffith v. City of Santa Cruz*, 207 Cal. App. 4th 982 (2012) ("*Griffith I*"), and *Griffith v. Pajaro Valley Water Management*

*Agency*, 220 Cal. App. 4th 586 (2013) ("*Griffith II*")[4]—do not support it. Those cases "involved large numbers of payors, who could rationally be (and were) placed in different usage categories, justifying different fees for different classes of payors." 243 Cal. App 4th at 1442. But where there are a relatively small number of payors—four in *Newhall*, twenty-six here, as opposed to thousands in *Griffith I* and *II*—the "concept of measuring proportionality 'collectively' simply does not apply," and "the only rational method of evaluating their burdens on, or benefits received from, the governmental activity, is individually, payor by payor." *Id.* at 1443.

Further, *Griffith I* involved regulatory fees, which are the subject of "a different exemption from Proposition 26," exception (e)(3). *Id.* at 1442-43. Regulatory fees are evaluated "collectively" because they may be "valid despite the absence of any perceived 'benefit' accruing to the fee payers." *Farm Bureau*, 51 Cal. 4th at 438 (citation omitted). It "makes perfect sense" that regulatory fees "'need not be finely calibrated'" because "it would be impossible to assess such fees based on the individual payor's precise burden on the regulatory program." *Newhall*, 243 Cal. App. 4th at 1443 (quoting *Griffith I*, 207 Cal. App. 4th at 997). But an agency cannot charge "collectively" for services or benefits that must be provided

[4] Met refers to *Griffith II* as *Pajaro Valley*, but *Newhall* calls it *Griffith II*, so San Diego does the same to dispel the confusion Met apparently wants to create. *See* 243 Cal. App. 4th at 1444-47; AOB at 57, 82-83.

"directly to the payor." *Id.* at 1444. That "cannot be, and is not, a 'fair or reasonable' allocation method." *Id.* (quoting Const. art. 13C, § 1(e)).

The *Newhall* court also rejected the argument—which, like Met, the Agency purported to base on *Griffith II*—that Proposition 26 was satisfied because "all retail purveyors benefit from imported water and the Agency's activities." 243 Cal. App. 4th at 1439, 1445-46. Costs must be allocated according to cost causation, not spread among customers "collectively" because, supposedly, "they all benefit." *Id.* at 1446. To hold otherwise "would effectively remove the proportionality requirement from Proposition 26. That we may not do." *Id.*; *cf.* AOB at 65, 81-83.

Here, as in *Newhall*, the number of Met member agencies is relatively small, but the variations among them in terms of cost causation are large. As Met explained to its bondholders in 2012: "Some agencies depend on Metropolitan to supply 100 percent of their water needs, regardless of the weather. Other agencies, with local surface reservoirs or aqueducts that capture rain or snowfall, rely on Metropolitan more in dry years than in years with heavy rainfall," while those "with ample groundwater supplies" rely on Met "to supplement local supplies or to recharge groundwater basins." 58-AR2012-16521. "Under these circumstances, allocation of costs 'collectively,' when the product is provided directly to each of the [twenty-six] payors, cannot be, and is not, a 'fair or reasonable' allocation method." *Newhall*, 243 Cal. App. 4th at

1444 (quoting Const. art. 13C, § 1(e)).

*Newhall*, while particularly apropos, is certainly not unique in supporting Judge Karnow's determination that Met's transportation rates violate Proposition 26. For example, in *Capistrano* (decided almost exactly a year after Judge Karnow issued his Phase I decision) the court analyzed Proposition 218's requirement that the "amount of a fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel." Const. art. 13D, § 6(b)(3). If that provision "is to mean anything," it implies "that there really *is* an ascertainable cost of the service that can be attributed to a specific—hence that little word 'the'—parcel. Otherwise, the cost of service language would be meaningless. Why use the phrase 'cost of the service to the parcel' if a local agency doesn't actually have to ascertain a cost of service to that particular parcel?" *Capistrano*, 235 Cal. App. 4th at 1505 (court's emphasis). That analysis applies *a fortiori* to Proposition 26's exception for a "charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product." Const. art. 13C, § 1(e)(2). There is no rational interpretation of that language to mean that the "local agency doesn't actually have to ascertain a cost of service to that particular" payor. 235 Cal. App. 4th at 1505.

Like Met, the defendant in *Capistrano* relied on *Griffith II*'s discussion of "the M-1 industry manual" and its "work-backwards-from-total-cost methodology in setting rates." *Id.* at 1514. But *Griffith II* "does not excuse water agencies from ascertaining the true costs of supplying water to various tiers of usage," and while it "may have noted that the M-1 manual generally recommends a work-backwards approach," it does not and cannot support "the proposition that a mere manual used by utilities throughout the western United States can trump the plain language of the California state Constitution." *Id.* The M-1 manual "cannot excuse utilities from ascertaining cost of service now that the voters and the Constitution have chosen cost of service." *Id.* That is especially damning to Met because Met's rates are based on the same backwards methodology *Capistrano* rejected. *See* AOB at 28-29, 67-68; 7-AA-1712 n.23; 9-AA-2309-2316; 26-AA-7175:6-24, 7212:2-13; 2-RA-372-87, 392-98.

The court in *Capistrano* found that "the precedent most on point," 235 Cal. App. 4th at 1511, was *Palmdale v. Palmdale Water District*, 198 Cal. App. 4th 926 (2011). Judge Karnow also relied on *Palmdale*, but Met ignores it completely—violating, again, its duty of candor to this Court. *See Hearn*, 247 Cal. App. 4th at 136-37. In *Palmdale*, the same Mr. Raftelis advised the defendant water district that allocating costs according to cost causation would jeopardize "rate stability." 198 Cal. App. 4th at 929. The water district—just like Mr. Raftelis's other client, Met—chose

rate stability over cost causation, but the Constitution requires the opposite. *See id.* at 938. As Judge Karnow aptly paraphrased, "*Palmdale* emphasizes cost causation, and bars unjustified price discrimination." 27-AA-7503.

*Bay Area Cellular Telephone Co. v. City of Union City*, 162 Cal. App. 4th 686 (2008), is yet another dispositive case that Met fails to mention. *See* 34-AA-9662 (relying on *Bay Area* in denying Met's new-trial motion). The *Bay Area* court held that a "fee for *access* to a governmental service is not the same as a fee for *use* of that service." 162 Cal. App. 4th at 698 (court's emphases). Otherwise, taxes "paid by the public to fund police or fire services available to all could be renamed 'public safety access fees' and be exempt from the voter approval requirements. Taxes paid to maintain city streets could be renamed 'road access fees.' The list of possibilities is endless," *id.* n.11, and it includes Met's System Access Rate, System Power Rate, and Water Stewardship Rate. Met charges for *access* to the SWP and to "water stewardship" (whatever that means), but those charges are not based on the *use* of any actual services. As Met finally admits on appeal, it "does not provide 'System Access' service, 'System Power' service, [or] 'Water Stewardship' service." AOB at 58.[5]

[5] Met makes that admission in the context of arguing that "the reasonableness of rates is properly measured at the service-rate level rather than at the individual-component level." AOB at 58. But that, like so many of Met's arguments, is refuted by *Newhall*, which invalidated a "rate component." 243 Cal. App. 4th at 1441. Met's argument on appeal also contradicts its original reason for unbundling its rates: "to reflect the

Met's arguments on appeal boil down to its assertion that "the key inquiry for a court in determining whether particular system-wide costs are properly included in a water rate is whether system users benefit *at all* from those costs." AOB at 82 (Met's emphasis). According to Met, because access to the SWP and "water stewardship" programs allegedly benefits "*all* of Metropolitan's member agencies, Metropolitan's decision to charge" *all* of those costs "to all users is reasonable." AOB at 81 (Met's emphasis); *see also id.* at 65. Met's assertions of universal benefits are unsupported, as Judge Karnow found based on substantial evidence. *See* 27-AA-7503-12. And, just as in *Newhall*, even if it were true that Met's member agencies "'all benefit' from the availability of supplemental water supplies," Met must allocate its costs according to cost causation, because to hold otherwise "would effectively remove the proportionality requirement from Proposition 26," which this Court "may not do." *Newhall*, 243 Cal. App. 4th at 1444.

On appeal, Met abdicates the requirements of cost causation,

---

different services provided by Metropolitan." 21-AR2010-5708. Perhaps Met "has some explanation for its change of tune, but the explanation is not to be found in the [138] pages of briefing [Met] has filed on appeal, nor did it surface in any way" below. *Hearn*, 247 Cal. App. 4th at 137. On the contrary, as Judge Karnow found, Met's position in its administrative record and at trial was that, in "order to accommodate a water transfer market, Metropolitan maintains an unbundled rate structure based on types of service provided. As a result, member agencies pay rates based on the services they use, and agencies that use the same service pay the same rate." 27-AA-7502 (quoting 58-AR2012-16587).

asserting that Judge Karnow "did not state the intended meaning of the term (used differently by the parties)." AOB at 113. Wrong. Judge Karnow explicitly stated that "cost causation" means that "Met must charge for its services based only on what it costs to provide them," ***and Met agreed***. 27-AA-7498; *see also, e.g.*, 34-AA-9589 ¶ 1; 27-AA-7493 n.65, 7503, 7507-08; 7405:1, 7406:27, 7413:19-28, 7429:11, 7431:5-8; 26-AA-7236:1. That definition, moreover, follows from the M-1 manual on which Met purports to rely. *See* AOB at 28-29, 67-68. "A basic principle inherent in the rate methodology contained in this manual is the concept of cost causation. Water rates are established so that users generally pay an amount equal or proportional to the costs the system incurs to provide them service." 15-AR2010-4185-86; *see also, e.g.*, 4-AR2010-1125; 15-AR2010-3997, 4123; 57-AR2012-16288_1757.

Judge Karnow rightly found that Met waived any attempt to back out of its admissions as to the applicability and definition of cost causation. 34-AA-9660. "The rule is well settled that the theory upon which a case is tried must be adhered to on appeal. A party is not permitted to change his position and adopt a new and different theory on appeal," because that "would not only be unfair to the trial court, but manifestly unjust to the opposing litigant." *Richmond v. Dart Indus., Inc.*, 196 Cal. App. 3d 869, 874 (1987) (quoting *Ernst v. Searle*, 218 Cal. 233, 240-41 (1933)). Cost causation was "the central focus of this case." 27-AA-7498. As Judge

Karnow found, to allow Met to change the focus now "would create exactly the wrong incentives: parties would be encouraged to try out one theory and then after it fails ask for a do-over based on a different theory." 34-AA-9660. That waiver finding is "binding on this court" because it is based on substantial evidence and the "inherent power to curb abuses and promote fair process." *Peat*, 200 Cal. App. 3d at 277, 288.

**c. Met's misallocation of SWP costs violates Proposition 26.**

Turning specifically to Met's SWP costs, Judge Karnow found that Met misallocates those supply costs to its transportation rates. Indeed, Met's own administrative record overwhelmingly proves that its SWP costs are supply costs, and that it only began to contend otherwise when it decided to overcharge San Diego for wheeling. *See* 27-AA-7504-09. As Judge Karnow found, nothing in the record justifies Met's misallocation of its SWP supply costs to its transportation rates. *Id.* at 7504.

Judge Karnow correctly rejected Met's argument that its SWP costs are transportation costs because "Met may from time to time use the state's transport capability to move some" of Met's water. *Id.* That does not and cannot "support the reasonableness of including **all** the state's transportation costs as part of Met's transportation costs. The record does not, for example, quantify the use of the state systems for Met's transportation, nor does it establish whether it is necessary for wheeling at all," nor does it establish any causal nexus between "costs associated with

the movement of water through the SWP's facilities" and the movement of water through Met's Colorado River Aqueduct. 27-AA-7504-05 (court's emphasis) (footnote omitted). Those findings are supported by substantial evidence, including the SWP Contract, under which DWR only charges Met "incremental costs" for wheeling. 2-AR2010-524-25, art. 55(b). Likewise, Met's experts at RMI explained that Met should only charge for "costs directly involved in the wheeling transaction" when delivering "non-Metropolitan water obtained by Member Agencies to offset deficient Metropolitan supplies." 5-AR2010-1248.

Judge Karnow also found that Met cannot justify its inclusion of SWP costs in its transportation rates on the basis that it blends SWP and Colorado River water. "The blend might be useful but, as to wheelers, the benefit is gratuitous, and not required by wheeling agreements." 27-AA-7504 (footnote omitted). Under the Exchange Agreement, for example, "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." 22-AA-6136 § 3.6. Further, the legislative blending requirement is irrelevant because it only applies to Met water, not third-party water. *See* Wat. Code. App. § 109-136; 43-RT-3006:13-20 (Yamasaki).

Lacking substantial evidence to support its transportation rates, Met resorts to misrepresentation. Met asserts that RMI's October 1995 report assigned SWP costs "to the 'Transmission Function,' *not* the "Supply

Function.'" AOB at 67 (Met's emphasis). But that is false. RMI's October 1995 report assigns the "costs of purchasing water from wholesale water suppliers" to the "Supply Function." 4-AR2010-1112. That includes water "purchased from . . . the State Water Project." 4-AR2010-1104.

In its December 1995 report, RMI confirmed that ***all*** SWP costs, specifically including the fixed costs and variable power costs that DWR includes in its "transportation charge," are "Supply Costs" for Met. 5-AR2010-1234; *see also* 5-AR2010-1233, 1245-46, 1249. Accordingly, Judge Karnow found, as a matter of fact supported by substantial evidence, that RMI's December 1995 report categorizes SWP costs as "Supply costs, including costs for the SWP to transport the water." 27-AA-7485.

RMI conveniently changed its tune in May 1996, after the Transfer Agreement between San Diego and IID had been announced, but Met omitted RMI's May 1996 report from the 2010 administrative record, and thus cannot rely on it as substantial evidence for its 2011-2012 rates. *See* 26-AA-7308-09 n.11; *cf.* AOB at 67. Even as to Met's 2013-2014 rates, the conclusory opinion on which Met relies is not substantial evidence, as Judge Karnow rightly found. *See* 27-AA-7483-86, 7505. The opinion in question is that DWR's transportation charges "are clearly transmission-related," and therefore are transportation costs for Met. 62-AR2012-16288_1876-77. As Judge Karnow explained, however, the "issue is not whether they are transportation related; the issue is whether there is any

reasonable basis to conclude they are ***Met's*** transmission charges. Unless I must accept as an adequate record any outside consultants' unsupported view (and I do not), this is insufficient." 27-AA-7505 (court's emphasis).

Judge Karnow was correct. Expert opinions are only "substantial evidence" to the extent those opinions are "supported by evidence in the record." *Roddenberry v. Roddenberry*, 44 Cal. App. 4th 634, 651 (1996). Unsupported conclusions "cannot rise to the dignity of substantial evidence." *Id.* (quoting *Pac. Gas & Elec. Co. v. Zuckerman*, 189 Cal. App. 3d 1113, 1136 (1987)). RMI's circular reasoning appears "to have emerged from the consultants' word processor without any thought." *Gonzales v. City of Santa Ana*, 12 Cal. App. 4th 1335, 1346-47 (1993). Judge Karnow was right to reject it. *See id.*; *Friends of Mammoth v. Town of Mammoth Lakes Redevelopment Agency*, 82 Cal. App. 4th 511, 557-58 (2000).

Judge Karnow also correctly rejected the same circular reasoning as it appeared in Mr. Raftelis's 2010 report, especially given Ms. Skillman's admission that she wrote that language for Mr. Raftelis's allegedly "independent" report, for purposes of this litigation. *See* 27-AA-7491-92, 7504; 1-RA-278-79; 31-RT-1930:11-1931:1; 1920:21-1921:1, 1926:20-1927:3, 1927:25-1930:10, 1935:2-9 (Skillman). Met's litigating position is unworthy of deference. *See Yamaha Corp. of Am. v. State Bd. of Equalization*, 19 Cal. 4th 1, 9-10 (1998). Given Met's reliance on an admittedly litigation-driven document, it was particularly appropriate for

Judge Karnow to make his own findings on this issue, as the *Farm Bureau* concurrence makes clear. 51 Cal. 4th at 447-48 (Moreno and Werdegar, JJ., concurring). Further, Ms. Skillman admitted at trial that Met's litigating position is inconsistent with the NARUC accounting standards Met purports to follow. *See* 27-AA-7493 n.65; 31-RT-1936:6-1943:21 (Skillman); 40-AR2010-11474; 1-RA-280; 57-AR2012-16288_1757; 1-RA-60. As this Court held in *Town of Tiburon v. Bonander*, 180 Cal. App. 4th 1057 (2009), cost allocations "must be both defensible and consistently applied." *Id.* at 1088. Met's are neither, as Ms. Skillman admitted, and as Judge Karnow found. *See* 27-AA-7504-05.

Met nitpicks Judge Karnow's statement that DWR's transportation costs 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." AOB at 69 (quoting 27-AA-7504). But there is nothing wrong with that analogy, which was meant to simplify the issues rather than complicate and confuse them, as Met's convoluted alternative does. *See id.* In any case, there is no point in debating Met's unwieldy analogy because the California Supreme Court already decided, in *Marquardt*, that the details about the SWP Contract that Met loads into its analogy are irrelevant. *Compare id.* with 59 Cal. 2d at 200-02.

As discussed above, the *Marquardt* court noted that the SWP Contract "has a slight resemblance to an agreement for the purchase of an

interest in a water system on the installment plan," but held nevertheless that it is actually "a contract for the furnishing of continued water service," under which Met "***does not obtain ownership of any facilities, ownership by the state being expressly provided for***." 59 Cal. 2d at 201(emphasis added) (citing 2-AR2010-216-17, arts. 17(f)(1)-(2)). "***Nothing in the contract indicates that the state shall hold title as a trustee or that the district shall be an equitable owner***." *Id.* at 202 (emphasis added).

Met never even cites *Marquardt*, violating its duty of candor yet again. *See Hearn*, 247 Cal. App. 4th at 136-37. Instead, Met misinterprets *Goodman v. County of Riverside*, 140 Cal. App. 3d 900 (1983), to overrule *Marquardt*. *See* AOB at 70-74. In addition to being wrong, that argument is waived, as Judge Karnow found. *See* 34-AA-9659-61. In any event, *Goodman* did not and could not contradict *Marquardt* to suggest that Met has an ownership interest in the SWP. *Goodman* also did not hold that Met "owns the costs" of the SWP, AOB at 103, unless that just means that Met must pay its SWP bills to ensure continued water service, and that the voters knew as much when they approved the SWP. *See Goodman*, 140 Cal. App. 3d at 907-10. Met's argument that it "owns the costs" of the SWP in some more significant sense was rejected as "unsound" and "unrealistic" in *Marquardt*—at Met's own request. 59 Cal. 2d at 200, 202.

**d. Met's Water Stewardship Rate violates Proposition 26.**

Met's Water Stewardship Rate is an unconstitutional tax, plain and

simple. While Met's SWP costs are real supply costs, and must be recovered as such, the Water Stewardship Rate does not recover any costs Met incurs to provide any service to its member agencies. As Met now admits, there is no such thing as "'Water Stewardship' service." AOB at 58. "Water Stewardship" is just Met's Orwellian term for its slush fund.

Even before Proposition 26, the law was clear that a rate "used to generate general revenue becomes a tax." *Farm Bureau*, 51 Cal. 4th at 438. Yet Devendra Upadhyay, Met's Water Resource Manager, admitted that Met puts the revenues from its Water Stewardship Rate into its "general reserves." 31-RT-1805:19-1808:14, 1848:24-1849:20 (Upadhyay). Met then uses those revenues as a carrot or a stick to reward or punish its member agencies. While some have received tens of millions of dollars in subsidies for their own local water supply projects, San Diego has only been getting the stick since it filed this lawsuit: "no new programs for local resource programs or desalination for San Diego." *Id.* at 1848:15-19. And, in addition to that obvious inequity, Met admits that it does not calculate the proportional benefits individual member agencies receive from the "water stewardship" subsidies or the projects they fund, individually or in the aggregate. 9-AA-2318, 2324, Admissions 20, 32. Met has not carried and, based on its own admissions, cannot possibly carry its burden of proving that its Water Stewardship Rate bears "a fair or reasonable relationship" to anything, let alone San Diego's "burdens on, or benefits

received from," Met's transportation of water under the Exchange Agreement. *See* Const. art. 13C § 1(e), final par.

Indeed, putting together the inconsistent positions Met has taken in its administrative record, at trial, and now on appeal, it is abundantly clear that Met's Water Stewardship Rate provides no benefits other than the money Met redistributes to reward or punish its member agencies. As Judge Karnow found, the record is full of Met's assertions that its "water stewardship" programs provide supply benefits, and thus "should be functionalized as 'supply costs.'" 27-AA-7510 (quoting 57-AR2012-16288_2179 (Raftelis)).[6] On appeal, however, Met emphatically asserts that its "water stewardship" subsidies have "***nothing to do with Metropolitan's water supplies***, which are imported from outside its service area." AOB at 81 (emphasis added). In other words, Met now admits that the Water Stewardship Rate does not provide Met or its member agencies any regional supply benefits, yet the subsidies funded by those payments do increase "local member agencies' water supplies"—but only to the extent Met decides to grant subsidies to any particular member agency. *Id.*

---

[6] *See also, e.g.*, 4-AR2010-1115, 1124; 5-AR2010-1249; 39-AR2010-11207-14; 39-AR2010-11257; 40-AR2010-11393-400; 57-AR-2012-16288_1744; 57-AR2012-16156-91; 57-AR2012-16215-16; 57-AR2012-16288_2179; 57-AR2012-16288_5291; 58-AR2012-16519; 22-AA-6157-64; 22-AA-6165-70; 22-AA-6171-83; 22-AA-6184-89; 2-RA-435:2-13; 25-AA-6932:3-22; 2-RA-489:11-490:19, 523:17-524:25, 525:16-527:19, 531:1-532:14, 542:17-543:24; 31-RT-1786:10-21, 1792:10-24, 1806:23-1807:8, 1832:21-1834:10 (Upadhyay).

That is the opposite of a "charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege." Const. art. 13C, § 1(e)(1). Met's cost allocations certainly do not bear a "fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity." *Id.* final par. Thus, the Water Stewardship Rate violates Proposition 26 by Met's own admissions.

As for alleged transportation benefits, Judge Karnow found that "the ***best*** we can do with this record," after reviewing it with deference to Met, "is to conclude that to some unspecified extent, some portion of the Water Stewardship Rate is causally linked to some avoided transportation costs. This is not enough to show that the costs of the service have a reasonable relationship to the service provided." 26-AA-7511 (emphasis added). That, standing alone, is fatal to Met's Water Stewardship Rate. *See id.* In the wheeling context, moreover, Met has not even shown benefits of "unspecified extent," *id.*, because its alleged "avoided costs attributable to the demand management programs relate to the transportation needs to provide purchased water," and are unrelated to wheeling. 26-AA-7512. And in every context, the purported transportation benefits are "at best indirect," and certainly not "'a specific government service or product provided *directly* to the payor that is *not* provided to those not charged.'"

*Newhall*, 243 Cal. App. 4th at 1441, 1451 (court's emphases) (quoting Const. art. 13C, § 1(e)(2)). There is simply no possible justification for Met's "allocation of 100% of these Water Stewardship Rate charges to transportation," which is "wholly arbitrary." 27-AA-7511.

Thus, Met has alternately failed to prove, or denied the existence of, any regional benefits from its Water Stewardship Rate, the illegitimate purpose of which is for Met to redistribute the money it collects like a reverse Robin Hood—or, rather, Prince John—to the member agencies Met favors. That violates principles "as old as Magna Charta [sic]." *Miller v. McKenna*, 23 Cal. 2d 774, 783 (1944) (citation omitted). It most certainly violates Proposition 26. *See, e.g.*, *Newhall*, 243 Cal. App. 4th at 1440-51.

**e. Met's attempts to evade Proposition 26 fail.**

Having effectively conceded that its transportation rates violate Proposition 26, Met argues that it does not apply. Met is wrong.

**(i) Met "imposes" its rates.**

Met first argues that Proposition 26 does not apply because it is framed in terms of charges that are "imposed," whereas Met contends that San Diego pays Met's rates "voluntarily" because Met is a "voluntary cooperative of member public agencies." AOB at 89 (citation omitted). Judge Karnow rejected Met's contentions based on findings of fact. *See* 27-AA-7499. Met concedes that those findings must be reviewed under the "highly deferential" test for "substantial evidence," but then ignores both

that standard and Judge Karnow's findings. *See* AOB at 56, 88-93.

As Judge Karnow explained, Met had the opportunity to present facts at trial to support its argument that it does not "impose" its rates on San Diego, but "Met did not adduce any such facts, whether from the administrative record, to which this claim is limited at Met's suggestion, or otherwise." 27-AA-7499. On the contrary, "the record contains numerous references to the fact that Met will 'IMPOSE RATES AND CHARGES.'" *Id.* (citing 23-AR2010-6159-162; 23-AR2010-6166-222; 23-AR2010-6223-239; 25-AR2010-6945-7029). "More substantively, the 2012 Official Statement to Met's bondholders confirms that SD had no choice but to use Met's facilities to wheel water." *Id.* (citing 58-AR2012-16509). Indeed, Met's official monopolistic policy precludes any "overlapping and paralleling governmental authorities and water distribution facilities to service Southern California." 7-AA-1926 § 4202(b).

Thus, as Met acknowledged when it unbundled its rates, the "ultimate consumer is captive within Metropolitan's system. This means that with respect to the purchase of imported water, a retail purveyor only has two choices; it can buy imported water from Metropolitan or it can acquire imported supplies from another source and have the water wheeled through the system." 1-RA-201. That and other substantial evidence supports Judge Karnow's finding that Met imposes its rates. *See* 27-AA-7499; 28-RT-1371:20-1372:4, 1375:7-21 (Cushman); 31-RT-1812:25-

1813:9 (Upadhyay); 2-RA-450:5-18 (Skillman).

Met's argument that it does not impose its transportation rates because San Diego is "free to acquire water from other sources," including conserved water from IID and "the All American and Coachella Canals," AOB at 90, is frivolous. That is precisely the water San Diego did acquire, but "had no choice but to use Met's facilities to wheel," as Judge Karnow found. 27-AA-7499. That finding, again, is amply supported by substantial evidence, including Met's own admissions. *See id.*; 1-RA-201; 31-RT-1812:25-1813:9 (Upadhyay); 2-RA-450:5-18 (Skillman).

Met argues that, by "definition, contractual price terms are not 'imposed,'" AOB at 90, but the nineteenth-century case Met cites for that proposition does not support it. *See Robinson v. Magee*, 9 Cal. 81, 83 (1858). On the contrary, *Robinson* held that a fundamental purpose of the Constitution is to guarantee contractual rights, rather than allow disputes to devolve into battles "among savage tribes of men." *Id.* "It is, therefore, the peculiar glory of our Constitution, that a single individual can successfully resist the claims of the whole community, when he is in the right." *Id.* So, too, a single Met member agency. The alternative, as the State Assembly Committee on Water wrote back in 1968, is to leave Met with no governing principles other than each member "seeking the greatest individual advantage for each member." 20-AA-5564. The Constitution prohibits such savagery. *Robinson*, 9 Cal. at 83.

Furthermore, Met's argument was explicitly rejected in *Williams Communications, LLC v. City of Riverside*, 114 Cal. App. 4th 642 (2003). The fee at issue there was found to have been "imposed" unlawfully because "the City would not grant the necessary permits without a license agreement, and would not enter into a license agreement without payment of the fee." *Id.* at 656. Likewise, Judge Karnow rightly found, based on substantial evidence, that San Diego had no choice but to pay Met's transportation rates to get its Colorado River water. *See* 27-AA-7499 (citing 58-AR2012-16509).

Met belatedly tries to close the legal barn door by attempting to distinguish *Bighorn-Desert View Water Agency v. Verjil*, 39 Cal. 4th 205 (2006), which held that water rates charged "as a result of the voluntary decisions of each water customer as to how much water to use" are "imposed." *Id.* at 216. Met argues that *Bighorn-Desert* only applies to retail rates. AOB at 92-93. As Judge Karnow observed, however, "the opinion does not appear to rely on the distinction argued by Metropolitan." 6-AA-1639. And *Newhall* has since confirmed that Proposition 26 applies to wholesale water rates. *See* 243 Cal. App. 4th at 1433-52.

**(ii) Met's arguments about the (e)(1) and (e)(2) exceptions are waived and wrong.**

Met also argues that its transportation rates fall within Proposition 26's exceptions (e)(1) and (e)(2). AOB at 94. But Met waived those

arguments by failing to present them at trial, as Judge Karnow found. 34-AA-9659-60. And Met is wrong in any case. Those exceptions require "a specific benefit," service, or product, provided "directly to the payor," that "is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit," service, or product. Const. art. 13C § 1(e)(1)-(2). "No such service or benefit is provided here," as Judge Karnow found based on substantial evidence—indeed, based on two trials and Met's motion for a third. 34-AA-9662. Further, the SWP and "water stewardship" costs charged to San Diego were found not to be reasonable in any event. *See* 27-AA-7452-7517.

**(iii) Exception (e)(4) does not apply and would not change the outcome if it did.**

Judge Karnow also correctly rejected Met's attempt to rely on exception (e)(4). *See* 6-AA-1640; 27-AA-7499. That exception applies to a "charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property." Const. art. 13C, § 1(e)(4). But the SWP and "water stewardship" costs at issue here have nothing to do with the use of Met's property.

***First***, SWP costs are not imposed for the use of Met's property. Once again, Met does not own the SWP; the State of California does. *See Marquardt*, 59 Cal. 2d at 200-02; 27-AA-7504-09; 9-AA-2330, Admission 44; 28-RT-1291:2-4; SWP Contract arts. 13, 17. Further, Proposition 26's

"exceptions all refer to activities directly undertaken by the local government." *Schmeer*, 213 Cal. App. 4th at 1327 n.5. But Met admits that it does not directly undertake any activities on the SWP. *See* 9-AA-2331-32, Admissions 45-47. Exception (e)(4) does not apply to SWP costs.

***Second***, Met's Water Stewardship Rate has nothing to do with using Met's property, but instead funds "recycling incentives," which is exactly the kind of charge the Legislative Analyst told the voters Proposition 26 would invalidate. 2-RA-405. The Legislative Analyst's statements to the voters are good evidence of voter intent. *Silicon Valley*, 44 Cal. 4th at 445.

***Third***, even if (e)(4) applies, which it does not, Met still "bears the burden of proving by a preponderance of the evidence" that its transportation rates do not exceed "the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity." Const. art. 13C § 1(e), final par. Met argues that "the (e)(4) exception requires no inquiry into the reasonableness of the charge." AOB at 101. As Judge Karnow correctly held, however, the requirements of the final paragraph apply "under *any* of the seven exceptions. Metropolitan has not provided authority for its alternative reading." 7-AA-1797 (court's emphasis). Met still has no authority for its alternative reading, *see* AOB at 101, and the cases interpreting Proposition 26 confirm that Met's reading is wrong. *See*,

*e.g.*, *Newhall*, 243 Cal. App. 4th at 1441, 1451 (applying the final paragraph independently of the exceptions); *Schmeer*, 213 Cal. App. 4th at 1327 n.5 (indicating that the final paragraph applies to all of the exceptions). Because Met has not carried its burdens under the final paragraph, its arguments about exception (e)(4) are immaterial.

**(iv) Met's Board is not the "electorate."**

Met's argument that its own Board is the "electorate" was refuted in *City of San Diego v. Shapiro*, 228 Cal. App. 4th 756, 770-93 (2014). Met only addresses *Shapiro* in a footnote, where Met tries to distinguish *Shapiro* on the basis that a city, "unlike Metropolitan, *has* a constituency of registered voters." AOB at 107 n.23 (Met's emphasis). According to Met, "the only body of people entitled or qualified to vote on Metropolitan's rates are the member agencies' representatives on Metropolitan's Board of Directors," so interpreting "electorate" as the court in *Shapiro* did "would repeal these statutory directives by implication." *Id.* at 105 (citing Wat. Code App. §§ 57 & 133). That is circular because it simply assumes what Met must prove: that Met charges proper rates rather than improper taxes.

Met also misstates Judge Karnow's ruling. Judge Karnow did not, as Met contends, "find an implied repeal," AOB at 106; he found exactly the opposite. "Interpreting the word 'electorate' to mean 'voters' does not repeal § 57; it simply reaffirms that Met's board can only approve otherwise lawful rates." 34-AA-9663. Neither Proposition 26, nor Judge

Karnow's interpretation of it consistent with *Shapiro*, repeal anything in the Met Act. Rather, Judge Karnow rejected Met's misinterpretations of both Proposition 26 and the Met Act. Rightly so, because Met has no "authority to exercise its discretion in a way that violates constitutional provisions or undermines their effect." *Silicon Valley*, 44 Cal. 4th at 448.

Moreover, Met's assertion that it has no "constituency of registered voters," AOB at 107 n.23, is false. Met has, in fact, sought and obtained approval for its bonds from "voters in Metropolitan's service area." 58-AR2012-16441. Met can do the same for taxes "in the manner required by law for the computation and collection of taxes for county purposes." Wat. Code App. § 109-311. Alternatively, Met may levy assessments if they comply with Proposition 218. Wat. Code App. §§ 109-134.5. What Met cannot do is levy illegal taxes and then claim that its own Board is the "relevant electorate." *See Shapiro*, 228 Cal. App. 4th at 770-93.

**(v) Proposition 13 is an alternative basis for affirmance, as Met effectively concedes.**

Furthermore, Met effectively concedes on appeal that Proposition 13 applies as an alternative basis for affirming the judgment. Previously, Met convinced Judge Karnow not to apply Proposition 13 based on *Brydon*, *see* 27-AA-7500, but *Brydon* has since been definitively overruled. *See Newhall*, 243 Cal. App. 4th at 1451 n.6; *Capistrano*, 235 Cal. App. 4th at 1512-13. Now, in relying on *Goodman*—a Proposition 13 case—Met

admits that Proposition 13 applies to Met's "transportation cost-allocation." AOB at 72; *see also* p. 55, *supra* (discussing *Goodman*); *Beaumont Inv'rs v. Beaumont-Cherry Valley Water Dist.*, 165 Cal. App. 3d 227, 234 (1985) (Proposition 13 applies to water facilities fees); *Capistrano*, 235 Cal. App. 4th at 1512-13 (*Beaumont* is good law; *Brydon* is not); 25-AA-6917:17-22 (Thomas, Met's designated witness on the Exchange Agreement, admitting that "Prop 13" applies to Met's charges). Thus, Proposition 13 also applies here, in addition to Proposition 26, as an alternative basis for affirmance.

**2. Judge Karnow correctly found, based on substantial evidence, that Met's transportation rates violate the Wheeling Statutes.**

**a. Standard of Review**

Met gets the standard of review wrong under the Wheeling Statutes for several reasons, first by asserting that this Court should ignore Judge Karnow's findings. AOB at 53. Again, in "reviewing a trial court's judgment on a petition for writ of ordinary mandate," this Court applies "the substantial evidence test to the trial court's factual findings." *Kreeft*, 68 Cal. App. 4th at 53; *accord, e.g.*, *Wong*, 137 Cal. App. 4th at 1382. Because those findings are based on substantial evidence—and Met does not argue otherwise, choosing to misstate the standard instead—they are "conclusive" and "binding" on appeal. *City of S. Gate v. Los Angeles Unified Sch. Dist.*, 184 Cal. App. 3d 1416, 1422, 1427 (1986).

As for the review of Met's wheeling rates—as distinct from Judge

Karnow's invalidation of them—section 1813 requires "written findings" based on "substantial evidence." Wat. Code § 1813. Met relies on Resolution 8520 as its "written findings." *See, e.g.*, 26-AA-7157:3-7158:14. As already discussed, however, that "conclusory resolution, which does not contain any evidence or factual information, does not constitute substantial evidence." *Livermore*, 184 Cal. App. 3d at 542.

Met tries to equate section 1813's "substantial evidence" standard with the "arbitrary and capricious" standard, AOB at 53-57, but the latter "is more deferential to agency decisionmaking than the substantial evidence standard." *Am. Coatings Assn., Inc. v. S. Coast Air Quality Dist.*, 54 Cal. 4th 446, 461 (2012). The Legislature chose the less deferential standard in section 1813 in response to Met's efforts to serve its own self-interest in setting wheeling rates. *See* 5-RA-1229. Met originally opposed the enactment of the Wheeling Statutes because the initial draft made the determination of the wheeling rate a quasi-judicial question for the State Water Resources Control Board (SWRCB) to decide. *See id.* Met objected to giving "SWRCB any role in determining fair market value for the use of facilities." *Id.* In response, the bill was amended to provide that the agency providing wheeling service would set the wheeling rate. 5-RA-1171. Given the absence of any independent review except in court, the bill was amended to provide that "the court shall consider all relevant evidence," as well as "the purposes and policies of this article," in deciding whether the

agency's "written findings" are supported by "substantial evidence." Wat. Code § 1813. As the Legislature recognized, the deference normally given to quasi-legislative decisions is inappropriate where, as here, the agency's "self-interest is at stake. A governmental entity can always find a use for extra money, especially when taxes do not have to be raised." *Valdes v. Cory*, 139 Cal. App. 3d 773, 790 (1983) (quoting *U.S. Trust Co. of New York v. New Jersey*, 431 U.S. 1, 26 (1977)).

Furthermore, whether Met is entitled to any deference depends on "*the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control*." *Yamaha*, 19 Cal. 4th at 14-15 (court's emphasis) (quoting *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944)). Those factors "have a much stronger influence than the words of the formula" for any particular standard of review, because "good judges customarily tread lightly when they are impressed with the care, conscientiousness, and balance of the administrators, but they penetrate more deeply, sometimes even substituting judgment, when the administrative performance seems to them to have been slovenly." *Cal. Hotel & Motel Ass'n v. Indus. Welfare Com.*, 25 Cal. 3d 200, 213 n.28 (1979) (citation omitted). Nevertheless, Judge Karnow did "tread lightly," and deferred to Met even though the record proves that Met did not act with "care, conscientiousness, and balance," and was worse than "slovenly." *Id.*;

*see*, *e.g.*, 27-AA-7471-72, 7503-12; 9-AR2010-2446-51; 1-RA-278-79; 31-RT-1930:11-1931:1; 1920:21-1921:1, 1926:20-1927:3, 1927:25- 1930:10, 1935:2-9 (Skillman). Met has nothing to complain about.

**b. Met's wheeling rates violate the principles of cost causation and intentionally discourage wheeling.**

As already noted, the Wheeling Statutes mandate that wheeling rates must be based on cost causation. Specifically, they prohibit rates that exceed "the reasonable charges incurred by the owner of the conveyance system, including capital, operation, maintenance, and replacement costs, increased costs from any necessitated purchase of supplemental power, and including reasonable credit for any offsetting benefits for the use of the conveyance system." Wat. Code § 1811(c). Only costs "attributable to the 'conveyance system' should be the basis for wheeling rates." 27-AA-7508.

Although "Met argues that the state's (DWR's) conveyance facilities are a part of Met's conveyance facilities," Judge Karnow, after carefully considering all relevant evidence, "with all deference to Met," found "no reasonable basis for this conclusion in the record." 27-AA-7508-09. In fact, far from showing any reasonable basis for Met's wheeling rates, the record proves beyond any doubt that Met failed to "act in a reasonable manner consistent with the requirements of law to facilitate the voluntary sale, lease, or exchange of water." Wat. Code § 1813.

Met admitted in Resolution 8520—its purported "written

findings"—that it allocates costs "attributable to Metropolitan's supply" to its wheeling rates "in order to protect Metropolitan's member agencies from financial injury by avoiding the shifting of those costs from a wheeling party to Metropolitan's other member agencies." 9-AR2010-2449 § 7; *see also* 8-AR2010-2450 § 13. Met tried to justify that approach by arguing that the Wheeling Statutes prohibit "injuring any legal user of water from that system, including financial injury." 9-AR2010-2447. But the court in *Morro Bay* explicitly rejected that misinterpretation of the Wheeling Statutes. *See* 81 Cal. App. 4th at 1050.

The plaintiff in *Morro Bay* was a school district that purchased most of its water from the City of Morro Bay, but entered into a water supply agreement with a third party, and sought to wheel that water through Morro Bay's system under the Wheeling Statutes. *See id.* at 1046-47. Like Met in its Resolution 8520, Morro Bay misinterpreted section 1810(d)'s reference to wheeling "without injuring any legal user of water" to prohibit "the rate increase it claims its other customers will have to bear if it loses the school district as a customer." *Id.* at 1050 (quoting Wat. Code § 1810(d)). But "the loss of income from a customer" is not "the sort of injury to a legal user of water the Legislature had in mind." *Id.*[7] The purpose of the

[7] This conclusion is amply supported by the legislative history, which shows that section 1810(d)'s language about "preventing injury to any legal user of water" was added to prevent "the loss of appropriation rights owned by the transferor by reason of the transfer." 7-AR2010-1724; *see also* 6-

Wheeling Statutes is "to reduce the cost of transporting water by taking advantage of excess capacity in existing systems." *Id.* at 1049. If doing so causes supply rates to go up, that just means supply rates had been too low, and adjusting them upward "does not amount to an injury." *Id.* at 1050.

Met only cites *Morro Bay* in passing, for the proposition that a writ of mandate "may not order the exercise of discretion in a particular manner unless discretion can be lawfully exercised only one way under the facts." AOB at 112-13 (quoting 81 Cal. App. 4th at 1051). Met fails to mention *Morro Bay*'s dispositive ruling, which establishes that Met's transportation rates are an abuse of Met's discretion, as Judge Karnow rightly found "under the facts." *Id.* Met fails to confront those facts—violating, once more, its duty of candor. *See Hearn*, 247 Cal. App. 4th at 136-37.

Because Met's wheeling rates violate the express provisions and policies of the Wheeling Statutes, they are "void and no protestations that they are merely an exercise of administrative discretion can sanctify them. They must conform to the legislative will if we are to preserve an orderly

---

RA-1414, 1421. In other words, transferors should not be penalized under the old "use it or lose it" doctrine. That has nothing to do with the notion that loss of revenue from customers who wheel third-party water "would ultimately mean higher charges to [the] remaining customers," 6-RA-1460-61, as is clear from the fact that opponents of wheeling continued to make that complaint long after the "injury" language was added. *See id*; 6-RA-1422. Indeed, Met itself unsuccessfully sought to amend section 1810(d) to redefine "injury" to include "shifting costs to any other users of the conveyance facility." 11-AR2010-3095 (underlining in original).

system of government." *Morris v. Williams*, 67 Cal. 2d 733, 737 (1967). Thus, Judge Karnow was right to invalidate Met's wheeling rates, along with its System Access Rate and Water Stewardship Rate, on which its wheeling rates are based. *See* 27-AA-7460, 7503-12, 7515-16.

### 3. Judge Karnow correctly found, based on substantial evidence, that Met's transportation rates violate section 54999.7(a).

With regard to Government Code section 54999.7(a), as elsewhere, Met is wrong to contend that this Court should decide Met's appeal "without reference to the superior court's findings." AOB at 53. The "substantial evidence test" applies to Judge Karnow's factual findings. *Kreeft*, 68 Cal. App. 4th at 53. Those findings establish, based on more than substantial evidence, that Met's transportation rates "exceed the reasonable cost of providing the public utility service." Cal. Gov't Code § 54999.7(a). Met does not seriously contend otherwise. Instead, Met argues that section 54999.7(a) does not apply. *See* AOB at 108-11. Met is wrong.

Met argues that section 54999.7(a) does not apply to wholesale water rates, but that makes no more sense in this context than it does in the context of Proposition 26, where it was refuted by *Newhall*. *See* 243 Cal. App. 4th at 1433-52. Section 54999.7(a) applies to any "fee, including a rate, charge, or surcharge, for any product, commodity, or service provided to a public agency" by another "public agency providing public utility service." Gov't Code § 54999.7(a). "Such a fee for public utility service,

other than electricity or gas, shall not exceed the reasonable cost of providing the public utility service." *Id.* The definition of "public utility service" includes "service for water." Gov't Code § 54999.1(h).

Met argues that, even though section 54999.7(a) applies, by definition, to "service for water," the list of other public utility services somehow suggests that "water" means "only retail water." AOB at 109. Nonsense. That list—which includes "flood control," for example—is not limited to "retail" services. Gov't Code § 54999.1(h). Met's argument also contradicts the broad definition of "public agency," which includes, among other federal and state agencies, any "district," any "public authority," and "any other political subdivision or public corporation of this state." Gov't Code § 54999.1(e). Met does not and cannot dispute that both parties here are "public agencies" under that definition, regardless of the fact that both provide "wholesale" water service to other agencies, which ultimately supply water to end users.[8]

Thus, there is no merit to Met's appeal of Judge Karnow's invalidation of Met's transportation rates based on section 54999.7(a).

---

[8] Met's assertion that "San Diego agreed" with Met's misinterpretation of section 54999.7(a) is false. AOB at 110. Mr. Raftelis, after admitting that section 54999.7 is "specifically" applicable to Met's rates, incorrectly asserted that Met is only required to do a cost-of-service study "every 10 years." 40-AR2010-11321. In response, San Diego's counsel noted that the reference to decennial studies in section 54999.7(c) is beside the point because Met's rates violate section 54999.7(a). 6-AA-1473.

### 4. Judge Karnow correctly found, based on substantial evidence, that Met's rates violate the common law.

Not even Met can deny that the common law applies to its transportation rates. Nor can Met deny that Judge Karnow applied the correct standard of review—he agreed to "give Met deference," presumed the reasonableness of Met's rates, and confined his review to Met's administrative record. 27-AA-7474. But deference is not a blank check. Under the common law, rates are invalid if they are not based "on the cost of service or some other reasonable basis." *Inyo*, 26 Cal. 3d at 159 n.4. Judge Karnow rightly concluded that Met's rates are unreasonable, even under the deferential common-law standard, based on factual findings grounded in evidence that is far beyond substantial. 27-AA-7455-7516. Met's response is to ask this Court to ignore those findings. *See* AOB at 53. Again, however, this Court applies "the substantial evidence test to the trial court's factual findings." *Kreeft*, 68 Cal. App. 4th at 53. Judge Karnow's findings easily pass that test, as already discussed at length.

### 5. Judge Karnow correctly found, based on substantial evidence, that San Diego is entitled to $235 million in damages and prejudgment interest under the Exchange Agreement.

#### a. Standard of Review

As discussed above, the Exchange Agreement provides 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." 22-AA-6137-38 § 5.2. In this context, the "applicable law" does not afford Met any deference. *See 300 DeHaro St. Inv'rs v. Dep't of Hous. & Cmty. Dev.*, 161 Cal. App. 4th 1240, 1256 (2008). Met "*chose* to enter into a written contract," giving the applicable law "a new legal identity: that of contractual language." *Id.* (court's emphasis). Met was contractually obliged to exercise its "discretionary power to fix rates" in "good faith and in accordance with fair dealing." *Id.* at 1253 (quoting *Cal. Lettuce Growers v. Union Sugar Co.*, 45 Cal. 2d 474, 484 (1955)).

Met certainly is not entitled to any deference with regard to Judge Karnow's finding that Met owes San Diego $235 million in contract damages and prejudgment interest. On the contrary, the "amount of damages" is "a fact question committed to the discretion of the trial judge," and "will not be disturbed if it is supported by substantial evidence." *Toscano v. Greene Music*, 124 Cal. App. 4th 685, 691 (2004). Similarly, Judge Karnow was entrusted with the discretion to decide whether Met carried its burden to reopen discovery. *See* Code Civ. Proc. § 2024.050(b).

Met cites *Toscano* for the proposition that the "measure of damages is a question of law subject to de novo review." AOB at 126. But the *Toscano* court was referring to the legal question of whether lost wages are recoverable on a promissory estoppel theory, and cited cases such as *Hurtado v. Superior Court*, 11 Cal. 3d 574 (1974), where the issue was

whether California or Mexico law applies. *See id.* at 579. Met raises no such issue, but challenges the amount of damages, which is a question of fact, as *Toscano* makes clear, citing *Westphal v. Wal-Mart Stores*, 68 Cal. App. 4th 1071 (1998), where the appellant was sanctioned because its arguments—like Met's—were frivolous in light of "the stringent standard of appellate review for claims of excessive damages." *Id.* at 1081.[9]

**b. Met breached the Exchange Agreement and caused San Diego's damages, as Judge Karnow found.**

The "applicable law" governing Met's charges under section 5.2 of the Exchange Agreement includes Proposition 26, the Wheeling Statutes, section 54999.7(a), and the common law. Mr. Thomas, Met's designated witness on the Exchange Agreement, admitted that "applicable law" includes "California law with regard to water rates and charges in general," including "Prop 13." 25-AA-6916:10-6917:22. And San Diego's lead contract negotiator, Scott Slater, testified that the parties agreed that the phrase "applicable law" would "capture the evolution in the law." 41-RT-2557:22-2558:25, 2559:20-2563:28; *see also* 1-RA-215-17.

Further, the parties plainly intended "applicable law" to include the Wheeling Statutes, which are all about "the conveyance of water," 22-AA-

[9] *See also, e.g., SCI Cal. Funeral Servs. v. Five Bridges Found.*, 203 Cal. App. 4th 549, 562 (2012); *New W. Charter Middle Sch. v. Los Angeles Unified Sch. Dist.*, 187 Cal. App. 4th 831, 843-44 (2010); *GHK Assocs. v. Mayer Grp.*, 224 Cal. App. 3d 856, 874 (1990).

6137-38 § 5.2, and which the Legislature enacted with the transaction consummated in the Exchange Agreement specifically in mind. *See* 5-RA-1216, 1258. Indeed, when Mr. Thomas was negotiating the Exchange Agreement, he explicitly informed Mr. Kightlinger—who is now Met's CEO and was then its General Counsel—that San Diego insisted on a "lawful wheeling rate," and would, if still necessary after five years, sue Met to obtain a rate "generally equivalent to the continuation of the exchange rate identified in the [1998] Exchange Agreement." 32-AA-9108 (quoting 1-RA-213). As discussed above, the rate in the 1998 Exchange Agreement was based on the Wheeling Statutes, pursuant to the Legislature's explicit instructions. *See* § I.B.3, *supra*.

Thus, as Judge Karnow succinctly put it, the Exchange Agreement may not be a "wheeling agreement," but its charges are "wheeling charges." 29-RT-1439:21-24; *see also, e.g.,* 1-RA-210-14, 218, 222-28, 259, 260-61, 262, 263-65; 40-RT-2407:19-21 (Cushman), 41-RT-2564:13-2568:25 (Slater), 42-RT-2865:11-2869:22 (Stapleton). Nevertheless, Mr. Kightlinger denied under oath at trial that Met agreed that San Diego could sue to obtain a lawful wheeling rate. *See, e.g.*, 41-RT-2682:10-25, 2672:6-19 (Kightlinger). But Judge Karnow explicitly and repeatedly found that Mr. Kightlinger lacks credibility. *See* 34-AA-9468:8-18 & n.12, 9469:23, 9484 n.39. This Court is "ill-equipped to decide this credibility issue independently (although substantial evidence plainly supported the

judgment on this point)." *Beasley v. Wells Fargo Bank*, 235 Cal. App. 3d 1383, 1395 (1991); *see also*, *e.g.*, *Lauderdale*, 67 Cal. App. 4th at 125; *Barboni v. Tuomi*, 210 Cal. App. 4th 340, 349 (2012). Judge Karnow's adverse credibility findings against Mr. Kightlinger are binding on appeal.

Moreover, Judge Karnow specifically invalidated the rates comprising Met's Price under the Exchange Agreement—its System Access Rate, System Power Rate,[10] and Water Stewardship Rate—based not only on the Wheeling Statutes, but also on Proposition 26, Government Code section 54999.7(a), and the common law. 27-AA-7516; 34-AA-9464.

---

[10] Met argues that Judge Karnow lacked the power to invalidate Met's System Power Rate because Met chose not to include that rate in the wheeling rate set forth in Met's administrative code, under which "wheelers pay only the 'actual cost (not system average) of power.'" AOB at 60 (quoting 7-AA-01938 § 4405). That argument is both nonsensical and disingenuous. Regardless of what Met's administrative code says, Met charges San Diego the System Power Rate under the Exchange Agreement. Judge Karnow found, and Met did not dispute, that the System Power Rate is one of the charges "generally applicable to Met's member agencies for the conveyance of water." 34-AA-9470. It was Met that convinced Judge Karnow, over San Diego's objection, to bifurcate the case and decide the validity of Met's System Power Rate, along with Met's other transportation rates, in the first phase. *See* 2-RA-388-91. And it was Met that chose, for its own benefit, to charge San Diego the System Power Rate under the Exchange Agreement, as opposed to the admittedly much lower actual cost of power on the Colorado River Aqueduct. *See*, *e.g.*, 1-RA-262; 276-77; 25-AA-6948:2-6949:8 (Thomas); 43-RT-2970:6-9 (Stapleton); 44-RT-3089:7-3093:10; 1-RA-276 (Lambeck). Met's calculated decision to charge San Diego more than the actual cost of power under the Exchange Agreement is no basis for its assertion that "the System Power Rate *cannot* be unfair to wheelers." AOB at 60 (Met's emphasis). On the contrary, it confirms that Judge Karnow was absolutely right to find that Met's System Power Rate *is* unfair to San Diego. *See* 27-AA-7504-09; 34-AA-9465-85.

There is "no dispute that those rates are the rates generally applicable to Met's member agencies for the conveyance of water." 34-AA-9470. Thus, because "Met's charges were not consistent with law and regulation, Met breached § 5.2 of the Exchange Agreement." *Id.*

Judge Karnow further found that "San Diego has established the fact of damages," based on evidence that is more than substantial. 34-AA-9473-75; *see also* 27-AA-7452-7517. For example, Dennis Cushman, San Diego's Assistant General Manager, testified "that San Diego has overpaid State Water Project and Water Stewardship Rate charges as a result of Met's rates." 34-AA-9473 n.17 (citing 40-RT-2396:9-24). And Met's own expert, Christopher Woodcock, admitted that San Diego "overpaid those charges." *Id.*; 5-RT-3196:22-3197:3 (Woodcock). None of Met's arguments "obviate the obvious point that San Diego has established the fact of damages." 34-AA-9473.

**c. San Diego proved damages of $188,295,602, and Met waived its contrary arguments, as Judge Karnow found.**

Judge Karnow also found, based on substantial evidence, that San Diego proved its damages in the amount of $188,295,602, and that Met waived any argument to the contrary. "San Diego computed its damages by removing the SWP costs and the Water Stewardship Rate from the Price." 34-AA-9476. "It is not possible to know how Met may in the future allocate" the disputed costs, but a "reasonable assumption is that the

entirety of the rate would have been moved. San Diego computed its damages under the contract for the 2011-2014 rate years using that assumption." 34-AA-9478.

Not only was San Diego's damages methodology reasonable, there was "no viable alternate methodology available." 34-AA-9477. "Met did not offer a competing computation," and it "asks too much of San Diego to require it to recalculate Met's rates with any useful degree of precision." 34-AA-9478. "For a very, very long time courts have allowed approximation of damages." 34-AA-9666. The law has always required "that the wrongdoer shall bear the risk of the uncertainty which his own wrong has created." *Allen v. Gardner*, 126 Cal. App. 2d 335, 340 (1954) (quoting *Bigelow v. RKO Radio Pictures*, 327 U.S. 251, 265 (1946)).[11]

Met tries to blame its own failure of proof on Judge Karnow, but that is nothing short of frivolous, as Judge Karnow made clear:

---

[11] As Judge Karnow noted, this principle is not only extremely well established in California law, but also was applied in a similar situation in *MCI Telecommunications Corp. v. F.C.C.*, 59 F.3d 1407 (D.C. Cir. 1995), which held that it is "inequitable to permit defendants who were in the best position to set their rates at lawful levels in the first place and who later had opportunities to correct those rates to avoid responsibility for those unlawful rates because the complainant [could not] establish an appropriate rate without making simplifying assumptions." 34-AA-9478; *see also, e.g.*, Civ. Code § 3517; *Meister v. Mensinger*, 230 Cal. App. 4th 381, 396-97 (2014); *Scheenstra v. Cal. Dairies, Inc.*, 213 Cal. App. 4th 370, 402 (2013); *Kashmiri v. Regents of Univ. of Calif.*, 156 Cal. App. 4th 809, 849 (2007); *DePalma v. Westland Software House*, 225 Cal. App. 3d 1534, 1544-46 (1990); *Benard v. Walkup*, 272 Cal. App. 2d 595, 605-06 (1969).

> Met claims my decision [not to reopen discovery] prevented it from pursuing expert discovery necessary to rebut San Diego's claimed damages, and was therefore inconsistent with well-recognized principles that a party can argue in the alternative. ***But this isn't true***. Met *was* allowed to make inconsistent allegations and arguments, but it failed to offer proof to support them. . . . ***Met's argument on damages is plainly waived***. . . . Met's claims now are based on brand-new damages calculations. They should not be considered in assessing whether damages were excessive. Based on the evidence I had as of the trial, the damages awarded were appropriate. At that time, there were no alternate methods presented, and San Diego's calculations were reasonable. ***Met refused to present a damages calculation or methodology because it hoped that its reasoning would actually lead to a dismissal***. Having seen that I did not dismiss, Met now reverses its position and wants to retry the case. As I note above, ***adopting Met's position now would create exactly the wrong incentives, profoundly threating the finality of trials and judgments***.

34-AA-9664-65 (bold emphases added; regular italics in original) (citations omitted); *see also* 27-AA-7632-34 & n.1 (Met failed to prove a basis for reopening discovery and "did not submit anything resembling a meet and confer declaration under C.C.P. § 2016.040"). Those findings are "binding on this court." *Peat*, 200 Cal. App. 3d at 277. Met's attacks on the damages award are frivolous and, indeed, sanctionable. *See Westphal*, 68 Cal. App. 4th at 1081-83.[12]

---

[12] *See also, e.g.*, *Mesecher v. Cty. of San Diego*, 9 Cal. App. 4th 1677, 1686 (1992) ("[W]here a deliberate trial strategy results in an outcome disappointing to the advocate, the lawyer may not use that tactical decision as the basis to claim prejudicial error."); *Lundquist v. Marine Eng'rs Beneficial Ass'n No. 97*, 208 Cal. App. 2d 390, 396 (1962) ("Unless a theory of damages is presented to the trial court it may not be considered on appeal.").

### d. San Diego is entitled to $46,637,180 in prejudgment interest, as Judge Karnow found.

Judge Karnow properly awarded prejudgment interest at the statutory rate because the Exchange Agreement "does not stipulate a legal rate of interest." Civ. Code § 3289(b); *see* 34-AA-9491-97, 9586 ¶ 2; 6-RA-1503-04. Although Met argued below that damages were not sufficiently certain for San Diego to recover prejudgment interest, Met has abandoned that argument on appeal. *See* AOB at 130-33. Met's only argument now is that section 12.4(c) of the Exchange Agreement stipulates a legal rate of interest. *See id.*

Met's argument is simply "not reasonable," and contradicts section 12.4(c)—which, as Judge Karnow found, does not stipulate any legal rate of interest (other than the statutory rate); which Met contended was a security provision; and which Met, in fact, treated as anything but a prejudgment-interest provision. *See* 34-AA-9492-93, 9665-66. Those findings were based on substantial evidence, including extrinsic evidence on which Met itself relied. *See* 27-AA-7619-24. Thus, Met's arguments about prejudgment interest fail. *See, e.g.*, *Hennefer v. Butcher*, 182 Cal. App. 3d 492, 500-02 (1986).

### e. The Exchange Agreement is not "illegal."

Met's argument that the price term in the Exchange "was deemed illegal," AOB at 124, is also frivolous. In fact, Judge Karnow held that it is

***not*** "illegal to require Met to set its charges for the conveyance of water pursuant to applicable law and regulation; precisely the opposite is true. The parties obviously bargained for—by definition—a *legal* price term." 34-AA-9483 (court's emphasis) (citing *Freeman v. Jergins*, 125 Cal. App. 2d 536, 546 (1954)). Judge Karnow was correct. In *South Tahoe Gas Co. v. Hofmann Land Improvement Co.*, 25 Cal. App. 3d 750 (1972), the court explicitly rejected the argument that a "contract was void because it provided for an illegal rate" where, as here, "the contract expressly, as well as impliedly," referred to the legal rate. *Id.* at 758. Moreover, "it would be a strange doctrine that would hold, in an action between the guilty party and the innocent parties, that the innocent parties are barred from affirmative relief because of such innocent participation. That is not and should not be the law." *Marshall v. La Boi*, 125 Cal. App. 2d 253, 268 (1954).

Met's argument is also estopped by the validation of the Exchange Agreement, at Met's own request, in the *QSA* litigation. There, Met moved for summary adjudication on the basis that the Exchange Agreement had been validated by operation of law, and the trial court agreed. *QSA*, 201 Cal. App. 4th at 838. As a matter of law, that adjudication of validity became "forever binding and conclusive" when all appeals were dismissed after remand, and Met is therefore "permanently enjoin[ed]" from arguing that the Exchange Agreement is invalid, including to this Court. Code Civ. Proc. § 870; *see also QSA Cases*, 237 Cal. App. 4th 72 (2015).

### 6. Judge Karnow correctly found, based on substantial evidence, that San Diego is entitled to preferential-rights credit for its payments under the Exchange Agreement.

Under section 135 of the Met Act, San Diego "shall have a preferential right" to Met water based on the amount it has paid Met over the years, excluding payments for the "purchase of water." Wat. Code App. § 109-135. Judge Karnow found, as a matter of fact, "that the Exchange Agreement was not an agreement pursuant to which San Diego obtained water from Met, but instead an agreement pursuant to which Met in effect conveyed water on behalf of San Diego." 34-AA-9488. Thus, "San Diego's payments under the Exchange Agreement must be included in the preferential rights calculation." 34-AA-9489. That finding is supported by substantial evidence, and Judge Karnow's interpretation of section 135 is correct. Met's arguments to the contrary have no merit.

Met's primary argument is that the preferential-rights issue here was already decided by *SDCWA v. MWD*, 117 Cal. App. 4th 13 (2004). But *SDCWA* merely held that Met's former "bundled" rate for Met water was for "purchase of water"; *SDCWA* had nothing to do with the Exchange Agreement, having been decided in the trial court long before the Exchange Agreement was executed. *See id.* at 24-26 & n.5. *SDCWA*, therefore, did not predetermine the answers to the questions Judge Karnow decided. *See* 34-AA-9485-89; 7-AA-1812-14.

Judge Karnow also correctly found that in "the pure wheeling

context, the wheeler does not purchase water from Met but pays a volumetric rate for Met to move water that belongs to the wheeler." 34-AA-9487. Met does not challenge that finding on appeal. *See* AOB at 133-38. Nor does Met challenge the resulting conclusion: "Wheeling payments must be included in the preferential rights calculation." 34-AA-9487.

As Judge Karnow found based on substantial evidence, the same conclusion applies to the Exchange Agreement. *See* 34-AA-9487-89 & n.46. "An exchange is the practical way which all water transfers are conducted. Unless you have a completely empty pipeline and aqueduct . . . all transfers are functionally executed through an exchange." 29-RT-1398:22-1399:2 (Cushman). As Judge Karnow found, under the Exchange Agreement, as in other wheeling transactions, "San Diego is not purchasing water from Met," but paying for the conveyance "of its own independent supplies." 34-AA-9488. That finding is well supported by the testimony of Met's own designated witness on preferential rights, Ms. Skillman, who admitted that "under the Exchange Agreement, the Water Authority pays for the delivery of its exchange water," which "is water that San Diego has obtained from the Imperial Irrigation District and the lining of canals," not from Met. 2-RA-567:11-569:11; *see also id.* at 568:22-569:4; 40-RT-2476:23-2477:5 (Cushman).

Judge Karnow also correctly rejected Met's counterfactual assertion that "the parties agreed that San Diego was purchasing Metropolitan

water." AOB at 137. In fact, for purposes of preferential rights, "the Exchange Agreement defines Exchange Water as Local Water, not Met Water." 34-AA-9487-88 n.44. That finding is amply supported by substantial evidence. *See id.*; 22-AA-6137 §§ 4.1-4.2; 2-RA-577:5-578:6, 581:11-582:17, 585:19-587:21 (Skillman).

Met argues that Judge Karnow's ruling "unfairly prejudices full-service water purchasers" because San Diego pays the "same rates" under the Exchange Agreement that "full-service water purchasers" pay. AOB at 138. Judge Karnow explained the illogic of that argument when he denied Met's motion for summary adjudication on preferential rights:

> The flaws in the reasoning include: (a) the components are not the same, for Price includes only some of the [charges full-service water purchasers pay]; (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."

7-AA-1814 (court's emphasis). It is not, as Met contends, "arbitrary and unfair to credit San Diego, but not others," for payments that are made by "San Diego, but not others." AOB at 138. Rather, it is arbitrary and unfair for Met to deny San Diego proper credit for payments that San Diego makes for everyone's benefit.

**7. Met's challenge to the writ of mandate is waived and meritless.**

Met's challenge to the form of the peremptory writ of mandate is both waived and meritless. Judge Karnow repeatedly asked Met for its

input on "specific wording which it would contend is consistent with the Statements of Decision," but Met "declined to offer anything." 6-RA-1507-09; *see also* 47-RT-3331:25-3332:25, 3342:23-3343:14. Having declined to offer any wording, Met "may not use that tactical decision as the basis to claim prejudicial error." *Mesecher*, 9 Cal. App. 4th at 1686.

In any case, there is nothing wrong with the writ. In *Carmel Valley Fire Protection District v. State of California*, 190 Cal. App. 3d 521 (1987), for example, the court upheld a writ over the State's objections that it violated the separation of powers. *See id.* at 533 n.7, 538-41, 551. A writ "is the correct method of compelling State to perform a clear and present ministerial legal obligation," including the statutory and constitutional obligation "to reimburse local agencies for state-mandated costs." *Id.* at 539. The "trial court was well within its authority," especially in light of the "State's manifest reluctance to reimburse" the plaintiffs. *Id.* at 551.[13]

[13] *See also, e.g., Cal. Ass'n for Health Servs. v. State Dep't of Health Care Servs.*, 204 Cal. App. 4th 676, 689-90 (2012) ("The trial court is directed to issue a supplemental writ of mandate compelling the Department to conduct a further rate review . . . in accordance with …[the law] and the provisions of this opinion."); *Conlan v. Bonta*, 102 Cal. App. 4th 745, 764 (2002) (directing trial court to issue a writ of mandate "ordering the Board to take further proceedings consistent with this opinion"); *Graham v. State Bd. of Control*, 33 Cal. App. 4th 253, 261 (1995) (directing trial court to issue a writ of mandate "directing the Board to . . . proceed in a manner consistent with this opinion"); *49er Chevrolet v. New Motor Vehicle Bd.*, 84 Cal. App. 3d 84, 93 (1978) (directing trial court to "issue a peremptory writ ordering the Department to vacate its decision and to conclude its administrative proceeding in a manner consistent with this opinion").

The cases on which Met relies are inapposite, addressing situations where the court had no jurisdiction to issue a writ,[14] or the plaintiff did not state a cause of action,[15] or there was nothing to enjoin.[16] None of that is true here, as Met's counsel conceded. *See* 47-RT-3331:25-3332:25. The only relevant case Met cites is *Morro Bay*, but the Court of Appeal there remanded for the trial court to "order the Morro Bay City Council to determine those matters listed in section 1812" of the Wheeling Statute and "retain continuing jurisdiction to assure compliance with its order." 81 Cal. App. 4th at 1051. No such remand is necessary or proper here because Judge Karnow, unlike the trial court in *Morro Bay*, did not erroneously dismiss the case, but instead properly conducted two full trials, and then issued an appropriate writ based on the law, detailed factual findings, and substantial evidence. *See id.*; 27-AA-7452-7517; 34-AA-9582-90.

Met complains that the writ goes beyond Judge Karnow's finding "that it was unreasonable to allocate *all* of Metropolitan's State Water Project transportation costs to conveyance." AOB at 114 (Met's emphasis). But Judge Karnow also found that Met previously allocated all of its SWP

---

[14] *See San Francisco v. Superior Court*, 53 Cal. 2d 236, 243-44 (1959); *Northridge Park Cty. Water Dist. v. McDonell*, 158 Cal. App. 2d 123, 125-26 (1958).

[15] *See McGinnis v. City of San Jose*, 153 Cal. 711, 715 (1908); *Gong v. City of Fremont*, 250 Cal. App. 2d 568, 572 (1967).

[16] *See Regents of Univ. of Cal. v. State Bd. of Equalization*, 73 Cal. App. 3d 660, 669 (1977); *Allen v. Bowron*, 64 Cal. App. 2d 311, 313-14 (1944).

costs "to supply, and ***none*** to transportation." 27-AA-7504 (emphasis added). "No reasonable basis appears in the record as to why this has changed." *Id.* Judge Karnow further found that Met does not own or operate the SWP or its transportation facilities; that Met does not transport SWP water from Northern California to the terminal reservoirs at Castaic Lake and Lake Perris; that the SWP is not part of Met's conveyance system; and that the SWP conveyance facilities are not part of Met's conveyance facilities. 27-AA-7456, 7504, 7508-09. Those findings are properly reflected in the writ of mandate, which contains the level of detail that Met itself requested. *See* 6-RA-1507-09; 34-AA-9588-90.

Thus, this Court should affirm the peremptory writ of mandate.

**8. Met's bonds are not a perpetual license to charge illegal rates.**

San Diego addresses last the argument Met places first. Met argues that its rates were validated in perpetuity because it allegedly pledged its "rate structure" as security for its 2002 bonds. *See* AOB at 42-52. That is perhaps Met's most frivolous argument, which is saying something.

The California Supreme Court explicitly rejected Met's argument in *Barratt American, Inc. v. City of Rancho Cucamonga*, 37 Cal. 4th 685 (2005). Even if new fees are substantially the same as previous ones for which the statute of limitations has expired, they are "subject to attack" when reenacted. *Id.* at 703. Otherwise, "if a fee was not challenged at its initial enactment, then the validity of all subsequent reenactments would be

immune to judicial challenge or review," and "there would be no effective enforcement mechanism to ensure that local agencies are complying with their duty to reduce the fees if revenues exceed actual costs," but instead "an incentive for local agencies to overvalue the estimated costs of services and then continually readopt that fee." *Id.*[17]

True to form, Met fails to address *Barratt*'s dispositive holding. Instead, Met relies on inapposite cases,[18] and contradicts its own representations to its bondholders. For example, Met relies on *Graydon v. Pasadena Redevelopment Agency*, 104 Cal. App. 3d 631 (1980), but there, the relief the plaintiff sought would have decreased revenues the defendant pledged to its bonds. *Id.* at 645-46. Here, Met told its bondholders exactly the opposite: "litigation challenging Metropolitan's rate structure" will ***not*** affect the security for Met's bonds, 5-AA-1118, which are "secured solely by a pledge of and a lien and charge upon the Net Operating Revenues." 5-AA-1116; *see also* 3-AA-683-86, 692. Although the challenged cost allocations determine how much each member agency must pay, it is a

---

[17] *See also, e.g., Travis v. Cty. of Santa Cruz*, 33 Cal. 4th 757, 770 (2004); *City of Ontario v. Superior Court*, 2 Cal. 3d 335, 340-477 (1970); *Miller v. McKenna*, 23 Cal. 2d 774, 782 (1944); *Arcadia Dev. Co. v. City of Morgan Hill*, 169 Cal. App. 4th 253, 262-64 (2008); *Fontana Redevelopment Agency v. Torres*, 153 Cal. App. 4th 902, 913 (2007).

[18] *California Commerce Casino, Inc. v. Schwarzenegger*, 146 Cal. App. 4th 1406 (2007), for example, bears no resemblance to this case because it was about an Assembly Bill that made clear, on its face, that the plaintiffs' claims were untimely. *See id.* at 1419-23.

zero-sum game: Met will "generate the same level of revenues" regardless of its "rate structure." 3-AA-692. Lawful cost allocations will result in a "corresponding increase in cost shared by Metropolitan's other member agencies," which is why those other agencies have joined in Met's appeal. 1-RA-281-83. But "***revenues would not be affected***," as Met explicitly represented to its bondholders. 5-AA-1118 (emphasis added).

Met's reliance on *Aughenbaugh v. Board of Supervisors*, 139 Cal. App. 3d 83 (1983), is likewise misplaced. There, the plaintiffs demanded a refund of charges that were imposed before the voters passed the relevant validating act. *Id.* at 87. But here, as Met told its bondholders: "Rates in effect in prior years are not challenged in this lawsuit." 5-AA-1118.

And in *Friedland v. City of Long Beach*, 62 Cal. App. 4th 835 (1998), the defendants "filed a validation action, complied with statutory requirements, and obtained a final judgment affirming the legality of these resolutions." *Id.* at 838. The only validation action Met ever filed relating to its transportation rates was *MWD*, which Met lost in the trial court, and then dismissed after appellate remand for a full trial, without ever obtaining any judgment of validity. *See MWD*, 80 Cal. App. 4th at 1437. In any event, San Diego does "not seek a refund of overcharges in past years," so Met's reliance on old rates is completely misplaced. *Regents of Univ. of Cal. v. E. Bay Mun. Util. Dist.*, 130 Cal. App. 4th 1361, 1387 (2005).

Finally, Met's perpetual-validation theory is also waived. Under

section 634 of the Code of Civil Procedure, if a party does not alert the trial court to a purported error in its statement of decision, "that party waives the right to claim on appeal that the statement was deficient in these regards, and hence the appellate court will imply findings to support the judgment." *In re Marriage of Arceneaux*, 51 Cal. 3d 1130, 1133-34 (1990). Moreover, a party waives an affirmative defense by failing to pursue it after the trial court overrules a demurrer. For example, in *DeCelle v. City of Alameda*, 221 Cal. App. 2d 528 (1963), the court held that the defendants "clearly waived their right to rely on" the statute of limitations when, after demurrer, they did nothing more than include a vague reference to it in their answer. *Id.* at 533.

After demurrer, Met never mentioned its perpetual-validation argument again until this appeal—even after San Diego twice put Met on notice of its waiver. *See* 27-AA-7394-7451; 28-AA-7704 n.6; 33-AA-9335 n.1; 34-AA-9443-60, 9499-9502. Met's argument, therefore, is waived. *See* Code Civ. Proc. § 634; *Arceneaux*, 51 Cal. 3d at 1133-34; *DeCelle*, 221 Cal. App. 2d at 533. To hold otherwise "would not only be unfair to the trial court, but manifestly unjust to" San Diego. *Richmond*, 196 Cal. App. 3d at 874 (quoting *Ernst*, 218 Cal. at 240-41).

Accordingly, this Court should reject Met's argument that its 2002 bonds amount to a perpetual license for it to charge illegal rates, along with the rest of Met's meritless arguments on appeal.

## II. SAN DIEGO'S CROSS-APPEAL

### A. STATEMENT OF THE CASE AND THE FACTS

#### 1. San Diego's RSI claim

As discussed above, Met imposes its unlawful Water Stewardship Rate on all of its member agencies, and then uses the proceeds to fund some member agencies' local-water-supply projects. Met doles out those subsidies without making any effort to align the benefits with the burdens of the Water Stewardship Rate, which is, therefore, a "wholly arbitrary" and unlawful tax, as Judge Karnow found. 27-AA-7511. But the Water Stewardship Rate is far worse in San Diego's case because Met has barred San Diego from receiving any new subsidies and terminated existing subsidy contracts, all in retaliation for filing this lawsuit.

Met positioned itself to impose that penalty on San Diego by adding its RSI clause to its subsidy contracts in 2004, admittedly in direct response to the possibility that San Diego might sue after the five-year litigation timeout expired in 2008, as the Exchange Agreement expressly permits. *See*, *e.g.*, 28-AR2010-7823-26; 1-RA-267-71, 272-75, 266; 42-RT-2726:25-2735:21 (Kightlinger). If any member agency challenges the legality of Met's rates, including in court, the RSI clause purportedly authorizes Met to terminate that agency's subsidy contracts. *See* 29-RT-1401:1-1402:12, 1407:9-1412:4, 40-RT-2412:27-2415:21 (Cushman); 31-RT-1845:23-1850:4 (Upadhyay); 42-RT-2726:25-2735:21 (Kightlinger).

For example, the RSI clause in the contract Judge Karnow quoted in his order states that if San Diego "file[s] or participate[s] in litigation or support[s] legislation to challenge or modify [the] Existing Rate Structure, including changes in overall rates and charges that are consistent with the cost-of-service methodology, Metropolitan may initiate termination of this agreement." 7-AA-1815 (quoting 3-RA-822 § 8). Met refuses to restore terminated benefits, even "if a court upholds a recipient's challenge to MWD's rates and finds the challenged rates to be illegal." 4-RA-1026.

Met imposed its RSI clause with the indisputable object of dissuading and penalizing challenges to its illegal rates. When San Diego challenged Met's rates, Met did what it had threatened. Invoking its RSI clause, Met terminated most of San Diego's existing subsidy contracts and barred San Diego from receiving future subsidies, yet continued to impose its illegal Water Stewardship Rate on San Diego. *See* 1-RA-286-95, 284-85; 29-RT-1407:9-1412:4, 40-RT-2415:22-2419:4 (Cushman); 31-RT-1845:23-1848:19, 42-RT-2771:27- 2773:28 (Upadhyay).

San Diego sought a declaratory judgment holding Met's RSI clause invalid and unenforceable under "the California constitution, statutory law and common law." 6-AA-1397 ¶ 104. Met's RSI clause violates the California Constitution by punishing San Diego for petitioning for redress of Met's unlawful and unconstitutional rates. Const. art. 1, § 3. It also violates California Civil Code section 1668, which prohibits contracts that

"have for their object, directly or indirectly, to exempt anyone from responsibility for his . . . violation of law, whether willful or negligent." Civ. Code § 1668. And it is unconscionable under the common law, violating not only San Diego's rights, but the rights of "its ratepayers, as well as Metropolitan ratepayers generally." 6-AA-1398-99 ¶ 108.

Judge Karnow, however, granted Met's motion for summary adjudication of San Diego's RSI claim. Judge Karnow held that, as a public agency, San Diego lacks standing to seek a declaratory judgment invalidating a contractual provision that was intended to, and does, burden San Diego's ability to challenge Met's illegal rates. 7-AA-1816-22. Judge Karnow based that conclusion primarily on *Star-Kist Foods, Inc. v. County of Los Angeles*, 42 Cal. 3d 1 (1986), which held that "subordinate political entities, as 'creatures' of the state, may not challenge state action as violating the entities' rights under the due process or equal protection clauses of the Fourteenth Amendment or under the contract clause of the federal Constitution." *Id.* at 6; *accord* 7-AA-1818. Judge Karnow also held that Civil Code section 1668 does not apply because, while the RSI clause clearly "*burdens* San Diego's ability to bring suit by increasing the costs of suit," it "does not exempt Metropolitan from liability." 7-AA-1829-30 (court's emphasis).

But Judge Karnow acknowledged that neither *Star-Kist* nor the other cases on which he relied directly support his conclusion that San Diego

lacks standing to assert its RSI claim. *See* 7-AA-1820-21. Accordingly, Judge Karnow addressed the merits of San Diego's RSI claim with "appellate review" in mind. 7-AA-1822. Judge Karnow found that, "if San Diego does have standing, it wins on the merits of the claim" because Met's RSI clause improperly burdens San Diego's right to seek judicial review of Met's unlawful rates. *Id.*

On December 8, 2015, San Diego timely cross-appealed the judgment against it on its RSI claim. 34-AA-9626-28. That judgment is appealable. *See* Code Civ. Proc. §§ 437c(m)(1), 904.1(a)(1).

**2. San Diego's attorneys' fees for Phase II**

Under the Exchange Agreement, San Diego had the absolute right, after the five-year peace treaty, to contest the charges that constitute Met's Price. 22-AA-6137-38 § 5.2. The parties further agreed that the prevailing party "shall be entitled" to recover its reasonable attorneys' fees "incurred in prosecuting or defending against such contest." *Id.* After prevailing under section 5.2, San Diego moved for attorneys' fees under section 5.2.

In its opposition to San Diego's motion, Met made "clear" that it was "not contesting the reasonableness of either the hourly rates or the number of hours spent by SDCWA's counsel on any particular project." 6-RA-1512. But Met argued that San Diego was only entitled to fees for the first phase of the case, in which Met's rates were invalidated. *See id.* at 1516-20. Judge Karnow agreed with Met, interpreting section 5.2 as a

"highly idiosyncratic" fee clause that did not cover the contract phase. 34-AA-9711-12. Accordingly, Judge Karnow reduced San Diego's fee award by $2,617,143.53—the amount the parties agreed San Diego reasonably incurred in the contract phase of the case. *See id.*; 6-RA-1520:16.

On April 19, 2016, San Diego filed its timely cross-appeal to the order partially denying San Diego's motion for attorneys' fees. 34-AA-9720-22. That order is appealable. *See* Code Civ. Proc. § 904.1(a)(2). On June 7, 2016, this Court consolidated the related appeals and cross-appeals.

## B. ARGUMENT

### 1. The standard of review is de novo.

San Diego's standing to challenge Met's RSI provision "is a question of law" that this Court reviews "de novo." *T.P. v. T.W.*, 191 Cal. App. 4th 1428, 143 (2011). Likewise, this Court interprets the attorneys' fee provision in the Exchange Agreement de novo because Judge Karnow's interpretation did "not turn on the credibility of conflicting extrinsic evidence." *Tribeca Companies, LLC v. First Am. Title Ins. Co.*, 239 Cal. App. 4th 1088, 1110 (2015).

### 2. San Diego has standing to challenge Met's RSI clause, which this Court should invalidate based on Judge Karnow's findings.

Although there is no case so holding, Judge Karnow ruled that San Diego "does not have an independent constitutional right to petition the legislature or the courts because that is an inherently individual right." 7-

AA-1821. The practical result of that decision is to give Met *carte blanche* to impose whatever penalties it can concoct on San Diego (or any other Met member agency) in explicit retaliation for having the temerity to challenge Met's unlawful rates—even if, as here, the challenge is successful. San Diego has been forced to pay Met's Water Stewardship Rate for years, even after being excluded from receiving the benefits Met's other member agencies receive in the form of "water stewardship" subsidies. It would be astonishing and deleterious to the public trust that a public utility like Met, which provides services that are a literal necessity of life to millions of people, could enforce a contract clause designed to insulate its illegal conduct from legislative or judicial review and to penalize another public agency for daring to challenge that conduct to vindicate its rights and those of its constituents.[19]

As discussed above, Judge Karnow primarily based his ruling on *Star-Kist*, but that case says nothing about a public agency's right to sue under the California Constitution; it is entirely about the enforceability of federal rights. *See* 42 Cal. 3d at 6. And even as to federal rights, *Star-Kist* held that the County of Los Angeles had standing to challenge a tax statute

[19] Judge Karnow stated that San Diego did not allege that it was "asserting the rights of its constituents," 7-AA-1821, but that is simply incorrect. San Diego alleged that declaratory relief is "necessary in order to protect the Water Authority and its ratepayers, as well as Metropolitan ratepayers generally." 6-AA-1398-99 ¶ 108.

based on the federal commerce clause. "State action cannot be so insulated from scrutiny that encroachments on the federal government's constitutional powers go unredressed." *Id.* at 9.

In other words, as to federal rights, *Star-Kist* stands for the proposition that in some cases it is essential to permit state public agencies to sue to remedy constitutional violations. And the logic underlying *Star-Kist* could not be more applicable here. As the court explained, where "there is a real possibility" that an unconstitutional "scheme" would go "unchecked absent challenge by those entities" that have an "unmistakable" interest in challenging it, those entities have standing. *Id.*

Here, Met's entire purpose in imposing its RSI clause was to create "a real possibility" that Met's unconstitutional rates "would have gone unchecked." *Id.* As discussed above, Met's RSI clause is designed to prevent and punish "litigation challenging Metropolitan's rate structure." 1-RA-284-85; *see also* § I.B.5, *supra*; 28-AR2010-7823-26; 1-RA-267-71, 286-95, 272-75, 266; 41-RT-1845:23-1850:4, 42-RT-2771:27- 2773:28 (Upadhyay); 42-RT-2726:25-2735:21 (Kightlinger); 29-RT-1401:1-1402:12, 1407:9-1412:4, 40-RT-2412:27-2419:4 (Cushman); 42-RT-2726:25- 2735:21 (Kightlinger). As one of Met's twenty-six member agency customers, San Diego has an unmistakable interest in challenging not only Met's unconstitutional rates, but the RSI clause whereby Met has retaliated against San Diego for its challenge to those rates—a challenge

that had merit and ultimately succeeded. *See, e.g.*, 40-RT-2412:27-2419:4 (Cushman).

Furthermore, unless San Diego "is given standing to raise the issue, it will be effectively removed from judicial review." *Driving Sch. Assn. of Cal. v. San Mateo Union High Sch. Dist.*, 11 Cal. App. 4th 1513, 1519 (1992). As Judge Karnow noted, the people who ultimately pay Met's unlawful rates undoubtedly have the constitutional right to challenge those rates in court, yet probably lack standing to challenge the RSI clause itself because "it does not appear those constituents are signatories to the contract at issue." 7-AA-1821-22. That is not, as Judge Karnow erroneously concluded, a reason to deny San Diego's standing, *id.*, but a compelling reason why San Diego must have standing. Otherwise, the burdens of Met's unconscionable RSI clause—and of Met's illegal rates, if left unchallenged due to Met's RSI clause—will "fall on a class of plaintiffs ill-prepared to bring the litigation." 11 Cal. App. 4th at 1519. Thus, San Diego has standing to challenge Met's RSI clause.

Because San Diego has standing, it "wins on the merits," as Judge Karnow found. *See* 7-AA-1822-28. Met's RSI clause violates the "unconstitutional conditions doctrine" established in *Robbins v. Superior Court*, 38 Cal. 3d 199 (1985). Met did not and cannot carry its "heavy burden" to show that its RSI clause does not impose unconstitutional conditions. 7-AA-1822, 1824 (citing *Robbins*, 38 Cal. 3d at 213).

Specifically, Judge Karnow found that Met failed to carry its burden of proving that the RSI clause reasonably relates to public benefits that outweigh the burdens imposed on San Diego, and that there are no alternative means to achieve those public benefits. *See* 7-AA-1822-28. Although Met claims an interest in not having to reevaluate its rates, "there is no reason to see that as any sort of substantial benefit, and certainly not a *public* benefit." 7-AA-1826 (court's emphasis). Met's argument "proves too much: as an eternal interest of any entity with a budget, it would act to justify any burden on the exercise of a constitutional right." *Id.* It is undisputed and indisputable, moreover, that Met could recover its revenues through a lawful system of rates and charges. 7-AA-1827. Met's preference for its unlawful "rate structure" is no justification for its RSI clause: "There is no showing that preserving the existing rate structure is a worthy end in and of itself." *Id.*

**3. Met's RSI clause is also invalid under Civil Code section 1668.**

Met's RSI clause also violates Civil Code section 1668, and Judge Karnow erred in holding that section 1668 does not apply. Section 1668 prohibits contractual terms that "have for their object, directly or indirectly, to exempt anyone from responsibility for his own . . . violation of law, whether willful or negligent." Civ. Code § 1668.[20] For example, in *Health*

[20] Although section 1668 refers to "contracts," not clauses, where "a contract has several distinct objects, of which one at least is lawful, and one

*Net of California v. Department of Health Services*, 113 Cal. App. 4th 224 (2003), the court applied section 1668 to invalidate a clause providing that remedies for "non-compliance with laws not expressly incorporated into this Contract, or any covenants implied to be part of this Contract, shall not include money damages, but may include equitable remedies such as injunctive relief or specific performance." *Id.* at 229 (emphasis omitted).

The law is clear that such an "exculpatory provision may stand only if it does not involve 'the public interest.'" *Id.* at 233 (quoting *Tunkl v. Regents of Univ. of Cal.*, 60 Cal. 2d 92, 96 (1963)). Indeed, "despite differences in the interpretation of the scope of section 1668, California courts have construed the statute for more than" a century "to at least invalidate contract clauses that relieve a party from responsibility for future statutory and regulatory violations." *Id.* at 235 (citing *Union Const. Co. v. W. Union Tel. Co.*, 163 Cal. 298, 314-15 (1912)). Accordingly, the court in *Health Net* held that the clause at issue there would be invalid even if it did not involve the public interest, because it sought "to exempt a party from liability for violations of statutory and regulatory law," and that it was invalid *a fortiori* because it did, in fact, "affect the public interest and thus cannot stand under *Tunkl*." *Id.* at 236, 244.

---

at least is unlawful, in whole or in part, the contract is void as to the latter and valid as to the rest." Civ. Code § 1599; *see also, e.g., Armendariz v. Foundation Health Psychcare Servs., Inc.*, 24 Cal. 4th 83, 124 (2000).

Judge Karnow held that this case is distinguishable from *Health Net* because "unlike the facts in *Health Net*, Metropolitan is not actually relieved of liability for damages." 7-AA-1830. But that sets the bar too high for San Diego, and too low for Met. Complete exemption from liability is not required. Even the "indirect" object of avoiding responsibility for violating the law is prohibited. Civ. Code § 1668. Where, as here, a public utility inserts a contract clause with the clear purpose of deterring lawsuits to hold that public utility accountable for its own illegal acts, that clause is unenforceable. *See id.* It is undisputed, and Judge Karnow found, that the RSI clause does exactly that: it "*burdens* San Diego's ability to bring suit by increasing the costs of suit [and] may 'deter' suit in the sense of reducing the odds one will be filed." 7-AA-1829 (court's emphasis).

Furthermore, Met cannot reasonably deny—and Judge Karnow expressly found—that the benefits it denied San Diego by invoking the RSI clause are "public benefits." 7-AA-1822-23. That, by the way, does not imply that the Water Stewardship Rate is lawful—it is not. But, having imposed that charge on all of its member agencies to provide subsidies, Met cannot legitimately deny that the public has an interest in those subsidies. *See id.* Judge Karnow acknowledged that *Health Net* asks "whether there is a 'public interest' which is inhibited by contested language," but failed to connect that dispositive question with his earlier affirmative answer to the

same question. 7-AA-1830 n.87; *cf.* 7-AA-1822-23.[21] This Court, like the court in *Health Net*, should "have no hesitation in concluding" that Met's RSI clause "affects the public interest" because it "deters, and makes more expensive" San Diego's efforts to protect the public interest. 113 Cal. App. 4th at 237; *see* 7-AA-1822-23, 1829-30.

This Court, therefore, should hold that Met's RSI clause is invalid and unenforceable.

**4. San Diego is entitled to the undisputed amount of $2,617,143.53 in attorneys' fees for the contract phase of the case.**

Under Civil Code section 1717, "where the contract specifically provides that attorney's fees and costs, which are incurred to enforce that contract, shall be awarded . . . to the prevailing party," that party "shall be entitled to reasonable attorney's fees in addition to other costs." Civ. Code § 1717(a). Where the judgment is a "simple, unqualified win" on the contract, the trial court has "no discretion" to deny attorneys' fees under section 1717. *Hsu v. Abbara*, 9 Cal. 4th 863, 876 (1995).

Here, the Exchange Agreement specifically provides for attorneys' fees for the prevailing party, and the fees San Diego incurred in the second phase of the case were "incurred to enforce that contract." Civ. Code §

---

[21] *CAZA Drilling, Inc. v. TEG Oil & Gas Co.*, 142 Cal. App. 4th 453 (2006), on which Judge Karnow relied, is inapposite because it did not involve the public interest or the actions of a public utility, but rather a contract between "business entities" allocating "the risk of economic loss in the event of a particular mishap." *Id.* at 469, 475; *cf.* 7-AA-1829 nn.83-84.

1717(a); *see* 22-AA-6137-38 § 5.2. The Judgment expressly states that San Diego is "the prevailing party," and therefore entitled to attorneys' fees under the Exchange Agreement. 34-AA-9586 ¶ 6. There is no dispute that San Diego obtained a "simple, unqualified win." *Hsu*, 9 Cal. 4th at 876; *see* 34-AA-9461-90. Thus, San Diego was entitled to its undisputedly reasonable attorneys' fees for Phase II, and Judge Karnow had "no discretion" to rule otherwise. *Hsu*, 9 Cal. 4th at 876.

Judge Karnow mistakenly concluded that the fees provision in section 5.2 is "highly idiosyncratic" and "narrowly drafted to cover attorneys' fees in cases challenging rates." 34-AA-9711-12. But here is what section 5.2 says: "In the event that SDCWA contests a matter pursuant to the foregoing sentence, the prevailing Party shall be entitled to recovery of reasonable costs and attorneys fees incurred in prosecuting or defending against such contest." 22-AA-6137-38 § 5.2. The "foregoing sentence" describes San Diego's absolute right to contest Met's rates after the end of the five-year peace treaty: "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." *Id.* San Diego contested "such charge or charges" in Phase II—indeed, aside from preferential rights, that was the whole point of Phase II. *See* 34-AA-9461-90. Judge Karnow did not cite any evidence to support his

misinterpretation of section 5.2 to exclude fees for San Diego's contest of "such charge or charges" in the phase of the case specifically devoted to section 5.2. *See* 34-AA-9711-12. There is no such evidence.

On the contrary, Mr. Thomas, Met's designated witness on the Exchange Agreement, frankly admitted that "Section 5.2 allows the Water Authority to do what it has done in this case." 25-AA-6954:21-6955:1. What San Diego did in this case, "pursuant to the foregoing sentence," was sue after the expiration of the five-year peace treaty to obtain contract damages and other relief from Met's overcharges. The fact that Judge Karnow agreed to bifurcate the case at Met's request, over San Diego's objections, *see* 2-AA-388-91, did not and could not change the fact that the entire case was a contest "pursuant to the foregoing sentence," as Mr. Thomas admitted—including the second phase in which San Diego's contract claims under section 5.2 were decided; not just the first phase. *See* 25-AA-6954:21-6955:1; 22-AA-6137-38 § 5.2.

Thus, Judge Karnow erred by reducing San Diego's attorneys' fees by $2,617,143.53 for the second phase of the case. *See* Civ. Code § 1717(a); *Hsu*, 9 Cal. 4th at 876. Met did not dispute the reasonableness of that amount. 6-RA-1512. This Court, therefore, can and should order Met to pay that additional amount without remand.

## III. CONCLUSION

For all of the foregoing reasons, this Court should affirm the

judgment, the damages award, and the writ of mandate; invalidate Met's RSI clause; and order Met to pay San Diego an additional $2,617,143.53 in attorneys' fees for the contract phase of the case.

Respectfully submitted,

Dated: August 3, 2016

KEKER & VAN NEST LLP

By: /s/ *Dan Jackson*
DAN JACKSON

Attorneys for Respondent and Cross-Appellant
SAN DIEGO COUNTY WATER AUTHORITY

**CERTIFICATE OF WORD COUNT**

**(Cal. Rule of Court 8.204(c)(4))**

This brief contains 27,902 words, not including the portions of the brief excluded from the word limit by California Rule of Court 8.204(c)(3).

Respectfully submitted,

Dated: August 3, 2016

KEKER & VAN NEST LLP

By: /s/ *Dan Jackson*
DAN JACKSON

Attorneys for Respondent and Cross-Appellant
SAN DIEGO COUNTY WATER AUTHORITY