

THIS AGREEMENT FOR LEASE OF REAL PROPERTY (WATER SYSTEM) ("Lease") is entered into between the City of Commerce, a municipal corporation ("Lessor"), and California Water Service Company (CWS), a California corporation ("Lessee") (collectively, the "Parties").

### RECITALS

WHEREAS, Lessor is authorized under California Constitution, article XI, section 9 and California Public Utilities Code sections 10001 et seq. To establish, own, operate, control and lease public works to furnish its inhabitants and businesses with public utilities, including water service; and

WHEREAS, Lessor provides water service to industrial, commercial and residential customers in the service area described in Exhibit A attached hereto (as such, the service area may change from time to time in accordance with this Lease (the "Service Area") and Exhibit B – Operating Standards; and

WHEREAS, Lessor is the owner of certain real property, easements and rights of way and those certain pipes, mains, pumps and appurtenant facilities (including without limitation buildings, pump houses, sheds and other structures) constituting all of Lessor's water system (the "Water System") within the Service Area as more specifically described in Exhibit A attached hereto; and

WHEREAS, Lessor owns and operates the Water System to provide water service to its inhabitants and, in doing so, incurs various financial costs and liabilities; and

WHEREAS, Lessor seeks to lease the Water System to a qualified operator and has received competitive proposals for such a lease from various entities; and WHEREAS, after due consideration of such proposals, including comments received at a duly noticed public hearing, the Lessor has determined that the Lessee is the most qualified to lease and operate the Water System; and

WHEREAS, Lessor desires to lease the Water System to Lessee, and Lessee desires to lease the Water System from Lessor, for the period and upon the other terms and conditions set forth herein.

### AGREEMENT

NOW, THEREFORE, in consideration of the mutual promises and covenants contained herein and for other good and valuable consideration, the receipt and adequacy of which the Parties hereby acknowledge, Lessor and Lessee hereby agree as follows:

#### **Section 1. Lease of Water System**

##### **1.1. Property Leased**

Lessor hereby leases to Lessee, and Lessee hereby leases and hires from Lessor, the Water System for the Term identified in Section 2, below and in

accordance with the provisions of this Lease. It is specifically recognized and intended by the Parties that Lessee shall not offer or perform any public utility service within the jurisdiction of the California Public Utilities Commission ("CPUC") by virtue of its execution of this Lease and the performance of its obligations hereunder. The Parties specifically recognize and acknowledge that neither one of them is dedicating itself or any of its respective properties (including the Water System) to render public utility water service to customers within the Service Area, but rather agrees to faithfully perform its obligations set forth in the provisions of this Lease. If either the CPUC or a court enters a final order or judgment ("Dedication Order") finding that either Party or their respective properties (including the Water System) has been dedicated in such a manner as to subject the Water System and/or either Party to the jurisdiction of the CPUC, then this Lease shall be terminated in accordance with the provisions of Section 15.6, below. Lessee is not leasing from Lessor any of Lessor's rights to produce ("Lessor's Groundwater Rights") groundwater adjudicated pursuant to the Judgment entered in the action entitled Central and West Basin Replenishment District vs. Adams, Los Angeles County Superior Court, Case No. C786656 ("Judgment"), and nothing contained in this Lease shall be construed as a lease of Lessor's Groundwater Rights by the Lessee.

**1.2. Lessee's Acceptance of Condition of Water System**

Lessee accepts the condition of the Water System, and hereby waives any claim as to any defect, whether patent or latent, in the condition of the Water System. Lessee acknowledges that it has had a reasonable opportunity to inspect the condition of the Water System prior to executing this Lease and that Lessee is not relying on any representation by Lessor as to the condition of the Water System other than those representations expressly set forth in this Lease.

**1.3. No Subleasing**

At no time during the Term of this Lease shall Lessee enter into any sublease of all or any portion of the Water System with any third party.

**Section 2. Term of Lease**

The term of this Lease ("Term") shall be ten years. The Term shall commence on the "Effective Date" as defined in Section 15, below.

**Section 3. Use of Water System**

Subject to the provisions of this Lease, and in particular the additional conditions regarding the Lessee's use of the Water System set forth in Section 5, below, Lessee shall lease the Water System for the sole purpose and use of furnishing water service on behalf of Lessor to all customers in the Service Area in accordance with Lessor's applicable rules, regulations and tariffs for water service that are in effect from time to time during the Term of this Lease, including such rules and regulations set forth in the Lessor's Municipal Code Chapter 13.16 and any subsequent amendments thereto.

## **Section 4. Rent**

Lessee shall make the following payments of rent ("Rental Payments") to Lessor:

### **4.1. Base Rent**

Lessee shall pay to Lessor an annual rent payment in accordance with the schedule outlined in Attachment " " ("Base Rent"). The Base Rent shall be paid in monthly installments, with the monthly payment due and payable on the first day of each month after the Effective Date of this Lease. Base rent shall be adjusted in the same proportion (plus or minus), as customer service rates approved by the City Council

### **4.2. Additional Rent**

- (a) Lessee shall pay to Lessor additional rent that is equal to \$200 per each acre of foot ("AF") of groundwater that the Lessee annually produces pursuant to Lessor's Groundwater Rights in excess of 2,000 AF of groundwater that Lessee uses to serve customers within the Service Area. No additional rent is owed by Lessee for groundwater produced and served by Lessee pursuant to Lessor's Groundwater Rights that amounts to 2,000 AF or less. The amount of groundwater produced and served by Lessee pursuant to Lessor's Groundwater Rights shall be determined as of each "Anniversary Date" (as that term is defined in Section 15.2 below). The additional rent owed under this Section 4.2 shall be paid by Lessee within thirty (30) calendar days after each Anniversary Date.
- (b) On or before May 2<sup>nd</sup> of each calendar year, , Lessee shall provide to Lessor documentation demonstrating the amount of costs annually incurred in the operation of the Water System in the following areas: (a) the energy or power used to operate the Water System ("Annual Energy Costs"), (b) the replenishment assessment ("RA") imposed by the Water Replenishment District of Southern California ("WRD") on the production of groundwater in the Central Groundwater Basin ("Annual RA Costs"), and (c) the supplemental imported or recycled water purchased from the Central Basin Municipal Water District ("CBMWD") or any other entity ("Annual Supplemental Water Costs"). Lessor shall have thirty (30) calendar days within receipt of the foregoing documentation to confirm the accuracy of the costs identified therein and to resolve any discrepancies relating thereto.
- (c) The Parties acknowledge and agree that the direct actions of the Lessee may result in operational savings on a per unit cost basis with respect to Energy Costs, Annual RA Costs and Annual Supplemental Water Costs. Within sixty (60) calendar days of the conclusion of the time period described in the last sentence of Section 4.2(b), above, Lessee shall pay to Lessor additional rent in an amount equal to (i) forty percent (40%) of the operational savings in Annual Energy Costs resulting from a decrease in the per unit energy cost identified in Exhibit C hereto, (ii) 40% of the operational savings in Annual RA Costs resulting in a decrease of the RA unit cost identified in Exhibit C hereto, and (iii) 40% of the operational

savings in Annual Supplemental Water Costs resulting from a decrease in the supplemental water unit cost identified in Exhibit C hereto, provided, however, that no additional rent shall be due under this Section 4.2(c) if the decrease in the costs referenced in this sentence is subject to the provisions of Section 6.1(g), below.

## **Section 5. Operation, Maintenance and Capital Improvements - Exhibit B**

### **5.6. Condition on Surrender**

Upon expiration of the Term or the termination of this Lease, Lessee shall surrender the Water System to Lessor in sound operating condition and in a state of repair that is consistent with prudent use and maintenance during the Term in accordance with customary utility standards, reasonable wear and tear excepted.

## **Section 6. Rates and Other Tariff Rules**

### **6.1 Rates**

- (a) The rates and charges to be imposed in connection with the water service to be provided by Lessee to the customers served by the Water System ("Water Rates") during the period from the Effective Date to the first Anniversary Date shall be those rates and charges set forth in Exhibit B hereto and amended from time to time by the City Council.
- (b) On or before May 2<sup>nd</sup>, sixty (60) calendar days prior to July 1<sup>st</sup> of each year, the Lessee shall submit a written notice to the Lessor that provides the Lessee's recommendation ("Annual Rate Recommendation") regarding the Water Rates that should be established pursuant to the applicable provision of the City's Municipal Code or other laws. The Annual Rate Recommendation shall include the following:
  - (i) An identification of the structure by which the Water Rates shall be classified. The classification structure shall divide the Water Rates into commodity or quantity rates, service connection charges and fire indicator service charges, unless the Lessee proposes a different classification structure. Lessee shall provide sufficient detail in the Annual Rate Recommendation regarding any such alternative classification system.
  - (ii) A breakdown of those costs actually incurred by Lessee during the preceding year in operating the Water System over which Lessee had no substantial control, which costs shall be limited to Annual Energy Costs, the Water Replenishment District's Replenishment Assessment, Supplemental Water Costs, and applicable taxes, license and permit fees (collectively, "Outside Costs"). The Annual Rate Recommendation shall also provide a breakdown of the

estimated Outside Costs that Lessee reasonably believes will be incurred in the upcoming year of operating the Water System, including an analysis of any significant increases or decreases in any Outside Cost that Lessee ' expects will occur.

- (iii) A breakdown of all costs other than Outside Costs and Rental Payments actually incurred by Lessee during the preceding year in connection with the performance of its obligations to operate and maintain the Water System as set forth in Section 15 of this Lease (collectively, "Lessee's O&M Costs"). The Annual Rate Recommendation shall also provide a breakdown of the estimated amount of the Lessee's O&M Costs that Lessee reasonably believes will be incurred during the upcoming year of operating the Water System, including an analysis of any increases in Lessee's O&M Costs that Lessee expects will be incurred due to increases in the Consumer Price Index -All Urban Consumers and Sewerage Maintenance published by the U.S. Department of Labor, Bureau of Labor Statistics ("CPI").
  - (iv) The actual amount of water served by the Water System to the Lessor's facilities identified in Exhibit F hereto during the preceding year and the amount of Outside Costs allocable to such water service. The Annual Rate Recommendation shall also provide the Lessee's estimate as to the amount of water to be served to the Lessor's facilities for the upcoming year and the estimated amount of Outside Costs allocable to that upcoming water service.
  - (v) A breakdown of the Rental Payments actually paid by Lessee during the preceding year and the estimated amount of Rental Payments that Lessee reasonably believes will be paid during the upcoming year of operating the Water System.
  - (vi) An identification of Lessee's reasonable rate of return on its investment represented by Lessee's O&M Costs and Rental Payments.
  - (vii) Information relating to:
    - (A). water rates and charges established in cities and other service areas that are comparable to Lessor and the Service Area and
    - (B) the weighted average rate increases or decreases most recently approved by the CPUC in comparable rate cases filed by Lessee.
  - (viii) Lessee's recommended Water Rates for each class of service identified in the Annual Rate Recommendation.
- (c) Within forty-five (45) calendar days of its receipt of an Annual Rate

Recommendation that contains the information set forth in Section 6.1(b)(i)-(viii) and any supporting documentation reasonably requested by the Lessor (the "Rate Review Period"), the Lessor's City Council shall review the Annual Rate Recommendation. If, in the sole discretion of the Lessor's City Council, the Water Rates set forth on the Annual Rate Recommendation are discriminatory, not protective of the health and safety of the customers in the Service Area, or not reasonable in light of all the financial information provided on Section 6.1(b), above, then the Annual Rate Recommendation shall be sent back to the Lessee for further consideration and revision (a "Rate Recommendation Rejection"). Either concurrently with or fifteen (15) calendar days after a decision by the City to adopt a Rate Recommendation Rejection, the City shall prepare and adopt the appropriate written findings that set forth the reasons for the Rejection ("Rejection Findings"). If the City Council does not vote for a Rate Recommendation Rejection, by the expiration of the Rate Review Period (the "Annual Expiration Date"), then the Water Rates identified in the Annual Rate Recommendation shall become effective, without any further act by either Party, upon the Anniversary Date.

- (d) If a Rate Recommendation Rejection occurs, the Lessee shall submit a revised Annual Rate Recommendation to the Lessor in a prompt and expeditious manner. Lessor shall consider the revised Rate Recommendation within the forty-five day Rate Review Period and in accordance with the requirements set forth in Section 6.1(b), above. Until the Lessor's City Council fails to reject a revised Annual Rate Recommendation within a Rate Review Period, the Water Rates shall remain unchanged. If the Lessor's City Council fails to reject a revised Annual Rate Recommendation prior to the expiration of a Rate Review Period, then the Water Rates identified in the revised Rate Recommendation shall become effective, without any further act of either Party, retroactive to the immediately preceding Anniversary Date. (The retroactive application shall be without any cost or interest to either the Lessor or customers in the Service Area.)
- (e) In cases of a natural disaster, act of God or act of war that substantially impairs the Water System, the Lessee may submit a request to Lessor for a change to the Water Rates ("Emergency Rate Request"), which Emergency Rate Request shall not be subject to the provisions of Section 6.1(a)-(d), above. An Emergency Rate Request shall be accompanied by documentation that reasonably supports the request. The Lessor's City Council shall have thirty (30) calendar days (the "Emergency Rate Review Period") to consider the Emergency Rate Request, by which time the Water Rate(s) identified in the Emergency Rate Request shall take effect as of the expiration of the Emergency Rate Review Period unless the

Lessor's City Council votes to reject the Emergency Rate Request prior to the expiration of that review period. If the Lessor rejects an Emergency Rate Request, it shall adopt, either concurrently or within fifteen (15) calendar days of its decision, the appropriate written findings that set forth the reasons why the Emergency Rate Request was either discriminatory, not protective of the health and safety of the customers in the Service Area, or not financially reasonable. Upon receipt of a rejection of an Emergency Rate Request from the Lessor, the Lessee may re-submit a revised Emergency Rate Request to the Lessee. The Lessor's review of a revised Emergency Rate Request shall conform to the process and time deadlines set forth in this Section 6.1(e). If the Lessor fails to reject a revised Emergency Rate Request within thirty (30) calendar days of the Lessee's submittal, then the revised Emergency Rate Request shall become effective, without any further act of either Party, retroactively to the date on which the initial Emergency Rate Review Period expired. (Such retroactive application shall be without cost or interest to either the Lessor or customers in the Service Area.)

- (f) Lessee may propose at any time between submittal of Annual Rate Recommendations an increase in the Water Rates that is directly attributable to an unexpected increase in an Outside Cost. Such a request shall be accompanied by documentation that reasonably supports the proposal. Such a request shall be considered by the Lessee's City Administrator or City Council within forty-five (45) calendar days of submittal by the Lessee ("Outside Cost Review Period"). If the Lessor does not reject the request within that time period, the Water Rate shall be deemed increased, effective as of the expiration of the Outside Cost Review Period, to the extent necessary to pass through the unexpected increase in the Outside Cost to the customers in the Service Area in a manner substantially similar to that permitted by the CPUC. If the Lessor rejects the request submitted pursuant to this Section 6.1(f) prior to the expiration of the Outside Cost Review Period, then the Lessor shall adopt, either concurrently or within fifteen (15) calendar days of its decision, the appropriate written findings that set forth the reasons why the request was discriminatory, not protective of the health and safety of the customers in the Service Area, or not financially reasonable. Upon receipt of such a rejection from the Lessor, the Lessee may submit a revised request for an increase in the Water Rates that is attributable to an unexpected, substantial increase in an Outside Cost. . The Lessor's review of such a revised request shall conform to the process and time deadlines set forth in this Section 6.1(f). If the Lessor fails to reject such a revised request within forty-five (45) calendar days of the Lessee's submittal, then the revised requested increase in the Water Rates shall become effective, without any further act of either Party, retroactively to the date on which the initial Outside Cost Review Period expired. (Such

retroactive application shall be without cost or interest to either the Lessor or customers in the Service Area.)

- (g) In between submittal of Annual Rate Recommendations, the Lessee shall promptly provide written notice to the Lessor of a decrease in an Outside Cost that is solely attributable to a five percent (5%) or greater decrease in the rates, prices or fees charged by the supplier of the commodity or the taxing agency (a "Decreased Outside Cost Notice"). Within thirty (30) calendar days of submittal of a Decreased Outside Cost Notice, the Lessor shall provide written notice to the Lessee as to whether the Lessee should submit a proposed decrease in the Water Rates attributable to the decrease in the Outside Cost. If the Lessor requests such a proposal, the Lessee shall propose, within thirty (30) calendar days of the date of Lessor's notice, a decrease in the Water Rates that passes through the resulting decrease in Outside Costs to the customers in the Service Area in a manner substantially similar to that permitted by the CPUC. If the Lessor does not reject the proposal within thirty (30) calendar days of receipt of that proposed decrease in the Water Rates, the proposal shall be deemed approved and the Water Rates so decreased effective immediately. If the Lessor does not request that the Lessee submit such a proposed decrease in Water Rates, then the Lessee shall make a payment of additional rent to the Lessor that is equal to the decreased amount of Outside Costs that occurred from the date of the Decrease Outside Cost Notice through the next Anniversary Date. Said payment shall be paid by Lessee within thirty (30) calendar days after that Anniversary Date.

## **6.2. Tariff Rules**

The initial tariff rules (including without limitation the standard form of agreements for extensions, connections and water service activities) to be imposed in connection with the water service provided to the customers served by the Water System shall be as set forth in Exhibit G attached hereto. Lessee may propose changes or amendments to, or modifications of (including additions and deletions), such tariff rules as it deems appropriate from time to time. Lessor shall reasonably consult with the Lessee with respect to any changes in the tariff rules that Lessor seeks to adopt. Lessor shall act on Lessee's requests for tariff changes within sixty (60) calendar days of the receipt of the request; provided, that in the event Lessor fails to so act within that stated time period, the requested tariff changes shall be deemed approved. Lessor shall act reasonably in considering the Lessee's proposed changes to the tariff rules, including giving due consideration to the consistency with the proposed tariff rule and Lessee's standard CPUC approved tariffs.

## **Section 7. Collections**

### **7.1. Retention of Collections**

Lessee shall be entitled to receive, keep and retain all proceeds of the billings and collections for water service provided through the Water System provided by Lessee during the Term ("Lessee's Billings"). Lessee shall bear the loss of any Lessee's Billings that are not collected.

**7.2. Transition Periods**

On or as near as practicable to the expiration or termination of the Lease, the Parties shall promptly, and with reasonable cooperation, determine the amount of billings relating to the water service furnished by Lessee during the Lease that remain uncollected ("Lessee's Uncollected Billings"). All Lessee's Uncollected Billings shall remain the property of the Lessee, and Lessee shall be solely responsible for collecting such billings.

**7.3. Cooperation**

To the extent either Party is collecting a bill (some or all of which is the property of the other Party), the collecting Party shall use reasonable diligence in its efforts to collect such bill. Each Party shall cooperate with the other Party in the collection of unpaid/delinquent accounts.

**Section 8. Sub-divider Installations**

All water pipeline, service connection or other appropriate extensions of the Water System that are required to furnish water service to individuals or subdivisions within the Service Area during the Term shall be undertaken and completed by Lessee in accordance with Lessor's applicable tariffs and extension rules and regulations. The cost of constructing such facilities shall be borne by the Lessor, not the Lessee. Lessee shall promptly provide to Lessor copies of all documentation relevant to such facilities, including applications, contracts and invoices. In the event that any contract for such a facility requires a refund or repayment to the customer, Lessor shall pay that refund. The provisions of this Section shall apply to contracts for such facilities executed after the Effective Date and to existing contracts assumed pursuant to Section this Lease.

**Section 9. Insurance**

Lessee shall procure and maintain, at its sole cost, during the Term the following minimum types and limits of insurance, with companies reasonably satisfactory to Lessor, and Lessee shall furnish Lessor with a certificate(s) of insurance evidencing such insurance:

- 9.1. Commercial or Comprehensive General Liability ("CGL") Insurance** with limits of not less than \$2,000,000 per occurrence and \$5,000,000 in the aggregate for bodily injury and property damage as well as separate limits in the same amount should apply to products-completed operations coverage and personal injury liability. This coverage should also include coverage a "broad form property damage" endorsement, blanket contractual liability coverage (including without limitation all liabilities assumed by the

named insured under the Agreement), a severability of interest clause, and coverage for independent contractors. To the extent the Lessee's work, or work under its direction, may require blasting, explosive conditions, or underground operations, the comprehensive or commercial general liability coverage shall specifically include coverage for such blasting, explosion, collapse, and/or underground hazards. Lessor and its officers, directors, agents, employees and consultants shall be specifically identified as an additional insured under this policy.

- 9.2. Workers' Compensation Insurance as required by laws and regulations applicable to and covering employees of Lessee engaged in the performance of the Agreement. This insurance shall protect the Lessee against all claims under applicable workers' compensation laws or federal acts, including claims for injury, disease, or death of employees which, for any reason, may not fall within the provisions of a workers' compensation law. This insurance shall include an "all states" endorsement. The Lessee shall require each subcontractor similarly to provide workers' compensation insurance for all of the latter's employees to be engaged in such work unless such employees are covered by the protection afforded by the Lessee's workers' compensation insurance.
- 9.3. Employers' Liability Insurance protecting Lessee against common law liability in the absence of statutory liability, for employee bodily injury arising out of the master servant relationship with a limit of not less than \$1,000,000 per occurrence. Lessor and its officers, directors, agents, employees and consultants shall be specifically identified as an additional insured under this policy.
- 9.4. Automobile Liability Insurance, including non-owned and hired vehicle coverage, with limits of liability of not less than \$1,000,000 per occurrence and in the aggregate. This insurance shall be written in comprehensive form and shall protect the Lessee against all claims for injuries to members of the public and damage to property of others arising from the use of motor vehicles, and shall cover operation on or off the Site of all motor vehicles licensed for highway use, whether they are owned, non-owned, or hired. Lessor and its officers, directors, agents, employees and consultants shall be specifically identified as an additional insured under this policy.
- 9.5. Occurrence-Based Coverage. All insurance required under this Agreement shall be written on an occurrence basis; "claims-made" policies will not be accepted.
- 9.6. Cancellation. All insurance policies shall provide that coverage afforded thereunder will not be canceled, reduced in coverage, or renewal refused until at least thirty (30) calendar days' prior written

notice has been given to Lessor and additional insureds by certified mail.

- 9.7. Primary/Non-Contributing. All insurance policies shall provide that the coverages are primary and non-contributing with regard to any other insurance maintained by the Lessor.
- 9.8. Excess Liability Policy. Lessee shall secure and maintain excess insurance coverage over and above all of the policies listed herein with limits of liability of not less than \$1,000,000 per occurrence and an annual aggregate of not less than \$2,000,000.
- 9.9. Qualifications of Insurers. All insurance required under this Agreement shall be written by insurers authorized to do business in the State of California and with a minimum Best's Insurance Guide rating of A:VII. Self-insurance will not be accepted.
- 9.10. Duration: All insurance shall be maintained continuously during the life of the Lease.
- 9.11. No Work Without Insurance: The Lessee shall not commence or perform any operation or maintenance of the Water System unless the Lessee have in full force and effect all required insurance.
- 9.12. Deductibles: All deductibles must be declared and approved by the Lessor. At the option of the Lessor, either the insurer shall reduce or eliminate such deductible as they relate to the Lessor and its directors, officers, employees, and agents, or the Lessee shall procure a bond guaranteeing payment of losses, investigation, claim and administration and defense expenses.
- 9.13. No Limitation of Liability: Nothing contained in these insurance requirements is to be construed as limiting the liability of the Lessee or the Lessee's sureties in any manner.

## **Section 10. Lessor's Representations and Warranties**

Lessor represents and warrants to Lessee that:

- 10.1. Lessor owns the Water System free and clear of all liens, security interests and other encumbrances, other than certain rights-of-way and easements that do not materially affect the use thereof.
- 10.2. Lessor has all necessary power and authority to execute, deliver and perform this Lease. Lessor has received all requisite consents and approvals with respect to its execution, delivery and performance of this Lease. This Lease constitutes a legal, valid and binding obligation of Lessor enforceable in accordance with its terms. The execution, delivery and performance of this Lease by Lessor does not materially conflict with or

result in a breach of or a default under any contract or other document previously executed by Lessor.

- 10.3.** The Water System is in sound operating and physical condition and has been maintained and operated by CWS under the previous lease agreement, in accordance with applicable laws and reasonably prudent utility maintenance and operating practices. Lessor has no actual knowledge of any fact relating to the condition, operation or maintenance of the Water System that has not been disclosed to Lessee in writing by Lessor that materially adversely affects the operation and maintenance of the Water System.

## **Section 11. Lessee's Representations and Warranties**

Lessee represents and warrants to Lessor that:

- 11.1.** Lessee is a corporation duly organized and existing under the law of the State of California.
- 11.2.** Lessee has all necessary power and authority to execute, deliver, and perform this Lease. Lessee has received all requisite consents and approval with respect to its execution, delivery and performance of this Lease. This Lease constitutes a legal, valid and binding obligation of Lessee enforceable in accordance with its terms. The execution, delivery and performance of this Lease by Lessee does not materially conflict with or result in a breach of or a default under any contract or other document previously executed by Lessee.
- 11.3.** Lessee possesses all of the necessary permits and governmental approvals to operate and maintain the Water System.
- 11.4.** Lessee is not a debtor in any bankruptcy proceeding filed or initiated under U.S.C. 11 U.S.C. Section 101 et seq.

## **Section 12. Indemnities**

### **12.1. Lessee's Indemnity**

Lessee shall hold Lessor, its governing body, officials, officers, employees and agents free and harmless of and from, and shall defend, indemnify and protect Lessor, its governing body, officials, officers, employees and agents, against, any and all liability, loss, claims, demands, damage, expense and costs of any kind or nature (including without limitation reasonable attorneys' fees and costs) arising out of or in any way connected with Lessee's actions or omissions regarding its obligations under the Lease, including without limitation Lessee's actions or omissions in operating and maintaining the Water System.

## **12.2. Lessor's Indemnity**

Lessor shall hold Lessee, its Board of Directors, officers, employees and agents free and harmless of and from, and shall defend, indemnify and protect Lessee, its Board of Directors, officers, employees and agents against, any and all liability, loss, claims, demands, damage, expense and costs of any kind or nature (including without limitation reasonable attorneys' fees and costs) arising out of or in any way connected with Lessor's actions or omissions regarding its obligations under the Lease.

## **12.3. Survival**

The indemnities set forth in this Section 12 shall survive the expiration of the Term or the termination of this Lease and the termination of Lessee's right to possession of the Water System.

# **Section 13. Opportunity to Cure; Limitation on Remedies; Arbitration**

## **13.1. Opportunity to Cure Defaults**

- (a) In the event that either Party shall fail to make any payment required under this Lease as and when due, or to obtain 'and maintain any insurance required by this Lease, there shall be no default under or breach of this Lease until such failure has continued for ten (10) days following receipt of notice from the other Party specifying such failure.
- (b) In the event that either Party shall fail to perform any of its other covenants or agreements contained in this Lease, there shall be no default under or breach of this Lease until such failure has continued for thirty (30) days following receipt of written notice from the other Party specifying such failure.
- (c) Notwithstanding Section 13.1(b), above, in the event a failure to perform cannot be reasonably cured within such thirty (30) day period, there shall be no default under or breach of this Lease unless such Party shall fail to commence and diligently proceed toward full performance of the cure within thirty (30) days following receipt of written notice from the other Party specifying such failure or such party shall fail to complete the performance of such cure within a reasonable period of time.
- (d) Notwithstanding Section 13.1 (a) through (c), above, if a Party's default results in a threat to the health and safety of the customers being served in the Service Area, then the non-defaulting Party, in its discretion, may claim an immediate default and avail itself of any remedy available under applicable law, including without limitation, engaging in self-help by performing emergency repairs to the Water System and/or suspending operation of the Water System. If the non-defaulting Party claims that a default so threatens public health and safety, then written notice shall be immediately provided to the other Party, and the Parties

shall reasonably cooperate with each other as to the actions necessary to eliminate the threat to public health and safety.

**13.2. Arbitration**

Except for the defaults identified in Section 13.1(d), above, in the event that any dispute, controversy or claim ("dispute") shall arise between the Parties with respect to any of the provisions of this Lease or the performance of the terms and conditions of this Lease by any Party, such dispute shall be settled by non-binding arbitration under the rules of the American Arbitration Association and by an arbitrator selected from the [Northern/Southern] California Judicial Panel of Arbitrators of J.A.M.S./ENDISPUTE ADR Professionals (or such other group of arbitrators as the parties shall agree to utilize). The cost of any such arbitration shall be borne equally by both parties, subject to Section 19.9. Judgment upon the award of the arbitrator may be entered in any court having jurisdiction thereof. Either Party may demand that arbitration proceed on an expedited basis, in which case the arbitrator shall set an expedited schedule.

**Section 14. Lessee's Bonds, Letters of Credit and Guarantees**

- 14.1.** Prior to or concurrently with the execution of this Lease, Lessee shall provide a written guarantee from California Water Service Group in the form attached as Exhibit H hereto.
- 14.2.** Prior to or concurrently with the execution of this Lease, Lessee shall provide a performance bond in a form satisfactory to the Lessor in its sole discretion in the amount of \$845,000 that ensures Lessee's performance of its obligations hereunder regarding operation and maintenance of the Water System.

**Section 15. Effective Date of Lease, Anniversary Date, Termination of Prior Operating Agreement, Lessor's Audit, and Early Termination**

- 15.1.** For purposes of this Lease, the term "Effective Date" shall mean the later to occur of (i) the date upon which a judgment becomes final in favor of Lessor in a validation action that the Lessor shall file pursuant to California Code of Civil Procedure Section 860 et seq., in which the Lessor seeks a judicial order validating the fully executed Lease and the deposit of rental payments under the Lease into the Lessor's general fund ("Validating Action") and (ii) receipt by the Lessor of a favorable ruling from the IRS to the effect that the execution of this Lease will not, in and of itself, result in the interest payable on the City of Commerce Joint Powers Financing Authority's outstanding Water Facilities Lease Revenue Refunding Bonds, Series 1994A being included in the gross income of the owners of such Bonds for federal income tax purposes (the "Favorable Ruling"). If the IRS issues a Favorable Ruling, but if a court of any jurisdiction enters a final order or judgment that denies the relief sought by the Lessor in a Validation Action (a "Denial

Order"), then the Lessor shall have the unilateral right to cause the Lease to commence despite the Denial Order. If the Lessor exercises that right, then the Lessor shall send written notice to the Lessee within thirty (30) days after the date of the Denial Order, and the date of that notice from the Lessor shall become the "Effective Date" of the Lease.

- 15.2.** For purposes of this Lease, the term "Anniversary Date" shall mean the date on which every one (1) full year expires after the Effective Date.
- 15.3.** Upon the Effective Date of this Lease, the Water System Operation and Maintenance Agreement originally signed by the Parties as of (the "Water System O&M Agreement") shall be deemed terminated, except the Parties' rights and obligations thereunder shall survive as to the following: (a) billing and collecting Pre-Lease Billings, (b) payment by one Party of any monies owed to the other Party as of the Effective Date, and (c) any failure by any Party to perform its obligations thereunder.
- 15.4.** Upon the third, sixth, ninth, and twelfth Anniversary Dates, the Lessor may perform an audit of the Lessee's compliance with the terms and conditions of the Lease. Lessee, at its cost and expense, shall cooperate with Lessor with respect to the audit, including but not limited to providing copies of documents reasonably requested by Lessor and making its personnel available to work with Lessor. Lessor shall complete the audit within sixty (60) calendar days after commencement. Upon completion of the audit, Lessor shall provide Lessee with written notice ("Audit Notice") of Lessor's acceptance of Lessee's compliance with the terms of the Lease, any alleged defaults by Lessee (which defaults shall be addressed pursuant to Section 13 of this Lease), or Lessor's termination of the Lease.
- 15.5.** Lessor may terminate this Lease prior to the expiration of the Term (a) without cause pursuant to an Audit Notice upon at least ninety (90) calendar days written notice, (b) upon Lessor's sale of the Water System, or (c) upon Lessee's breach or default under this Lease that is not cured within the time period(s) identified in Section 13, above. Lessee may terminate this lease upon Lessor's breach of or default under this Lease that is not cured within the time period(s) identified in Section 13, above. In the event that this Lease is terminated for any reason prior to the expiration of the Term, then the Party terminating the Lease shall provide the other Party within written notice thereof (a "Termination Notice"). Within at least ninety (90) calendar days of issuance of a Termination Notice, (i) the Lease shall be deemed terminated ("Termination Date"), (ii) Lessee shall surrender possession of the Water System, including copies of all pertinent books and records, to Lessor; (iii) Lessee shall provide a written list of all accounts receivable from customers in the Service Area, which receivables shall remain the property of Lessee; (iv) Lessee shall pay to Lessor any Rental Payments owed under Section 4 of this Lease, as prorated for the portion of the period between the Termination Date and the next Anniversary Date.

- 15.6.** This Lease shall be deemed terminated, without any act of either Party, within thirty (30) calendar days of any Dedication Order, as that term is defined in Section 1.1 above.

## **Section 16. Sale of Portions of Water System**

### **16.1. Sale of Water System Properties**

In the event that Lessor determines to sell a portion or all of the Water System, Lessor shall notify Lessee in writing, describing the property in reasonable detail and specifying the costs and expenses that would be incurred by Lessee in removing or disconnecting such property from the balance of the Water System. Within thirty (30) calendar days of sending any such notice to Lessee, Lessor may sell all or a portion of the Water System as are specified in such notice.

### **16.2. Payment of Net Proceeds to Lessee**

If Lessor sells a portion or portions of the Water System pursuant to Section 15.1, Lessor shall apply the proceeds of such sale(s) first to reimburse Lessee for the costs and expenses of removing and disconnecting such portion(s) of the Water System. Any remaining portion of the sale proceeds shall belong solely to the Lessor.

## **Section 17. Service Area**

- 17.1.** Lessor shall not seek to materially expand or contract the Service Area without the Lessee's written consent, which consent shall not be unreasonably withheld.
- 17.2.** Lessee shall not compete with Lessor for customers in the Service Area and shall not construct any Lessee-owned capital facilities in the Service Area.

## **Section 18. Nondiscrimination**

Lessee represents and warrants that it shall not discriminate against any person or group of persons on account of sex, race, color, creed, national origin or ancestry in connection with the operation of the Water System or the furnishing of water service to customers within the Service Area. In connection with this Lease, Lessee shall conform to the requirements of the California Fair Employment and Housing Act, the regulations promulgated by the Fair Employment and Housing Commission to implement said Act, and all applicable federal, state and local nondiscrimination, affirmative action and equal employment opportunity law and regulations.

## **Section 19. Access**

- 19.1.** Throughout the Term and for three (3) years after the Lease expires or is terminated, Lessor shall have access to all of Lessee's financial, operating, maintenance, property, customer, complaint and other records, reports, maps or files that apply to Lessee's leasing, operating or maintaining of the

Water System. Lessor shall have such access after providing three (3) calendar days written notice to Lessee and during normal business hours at Lessee's headquarters or such other premises where such materials are maintained. Lessee may require the reproduction or electronic transfer of at Lessor's cost of Lessee's records, reports, maps or files.

- 19.2.** Throughout the Term, Lessor shall have access to any part of the Water System upon providing three (3) calendar days written notice to Lessee. However, Lessor shall take no action during such access that materially interferes with Lessee's operation, possession or quiet enjoyment of the Water System.

## **Section 20. Miscellaneous**

### **20.1. Notices**

All notices relative to this Lease shall be given in writing and shall be sent by confirmed facsimile transmission, overnight courier, registered or certified mail, postage prepaid, and addressed to the party to whom such notice is given at the following respective addresses:

To Lessor: CITY OF COMMERCE  
Attention: City Administrator  
2535 Commerce Way  
Commerce, CA 90040

To Lessee: California Water Service Company  
Attention: President  
1720 North First Street  
San Jose, CA  
95112-4598

Notices shall be deemed to be received at the earlier of the date of receipt or three (3) business days after the date of mailing, whichever is earlier.

### **20.2. Paragraph Headings**

Paragraph headings in this Lease are for convenience only and are not a part of this Agreement and do not in any way limit or amplify the terms and provisions of this Lease.

### **20.3. Compliance With All Laws and Governing Law**

In performing its obligations under this Lease, each Party shall comply with all applicable federal, state and local laws, regulations and permits. Further, this Lease shall be interpreted and enforced in accordance with the laws of the State of California.

### **20.4. Warranty of Authority**

The Parties warrant to each other that the individual executing this Lease on its behalf is duly authorized to execute and deliver this Lease on behalf

of that Party.

**20.5. Waiver of Default**

The failure of any Party to enforce against another provisions of this Lease, shall not constitute a waiver of that Party's right to enforce any provisions at a later time, and shall not serve to vary the terms of this Lease.

**20.6. Time**

Time is of the essence in this Lease.

**20.7. No Assignment**

This Lease shall not be assigned by any Party, without prior written consent of the other Party, which consent shall not be unreasonably withheld; provided, however, that Lessor's consent shall not be required in connection with any assignment by Lessee of all of its rights and obligations hereunder to an affiliated company which is controlled by, controls, or under common control with, Lessee; provided, further, that Lessor's consent shall not be required in connection with any assignment (whether or not as collateral) of Lessee's rights to payments hereunder.

**20.8. Binding Effect**

The rights and obligations of this Lease shall inure to the benefit of, and be binding upon, the Parties and their successors and permitted assigns.

**20.9. Attorneys' Fees**

In any action (including without limitation any arbitration) related to this Lease, the prevailing party shall be entitled to recover its attorney's fees and court costs and other nonreimbursable litigation expenses, such as expert witness fees and investigation expenses.

**20.10. Merger and Modification**

This Lease sets forth the entire agreement between the parties with respect to the subject matter hereof, and supersedes all prior oral or written agreements, representations, promises and negotiations. This Lease may be modified or terminated only in a writing signed by the Parties.

**20.11. Severability**

If any provision of this Lease is invalid or unenforceable with respect to any Party, the remainder of this Lease or the application of such provision to persons other than the person as to whom it is held invalid or unenforceable shall not be affected and each provision of this Lease shall be valid and enforceable to the fullest extent permitted by law.

**20.12. Interpretation and Execution**

This Lease is the product of negotiation and therefore shall not be construed against any party. This Lease may be executed in counterpart, each of which shall be deemed an original and all of which shall be deemed one and the same instrument.

IN WITNESS WHEREOF, the parties thereto have executed this Lease on the day and year first-above written.

LESSOR: CITY OF COMMERCE

By\_\_\_\_\_

Title,\_\_\_\_\_

LESSEE: California Water Service  
Company

By\_\_\_\_\_

Title\_\_\_\_\_