



STAFF REPORT

TYPE MEETING:	Otay Water District Board Meeting	MEETING DATE:	June 1, 2011
SUBMITTED BY:	Joseph R. Beachem, Chief Financial Officer	W.O./G.F. NO:	DIV. NO.
APPROVED BY: (Chief)			
APPROVED BY: (Asst. GM):	German Alvarez Assistant General Manager, Finance and Administration		
SUBJECT:	Substitution of the Letter of Credit for the Outstanding Variable Rate Debt		

GENERAL MANAGER'S RECOMMENDATION:

That the Board adopts Resolution No. 4172 approving the form of documents required for a substitution of the Letter of Credit (LOC) for the outstanding variable rate debt, approve the Bond Counsel Agreement, and authorizing the General Manager to execute the documents.

COMMITTEE ACTION: \_\_\_\_\_

See Attachment A.

PURPOSE:

To obtain approval by the Board to amend the Installment Sale Agreement for the 1996 Variable Rate Demand Certificates of Participation, to execute a Reimbursement Agreement with Union Bank in connection with substitution of the existing letter of credit securing the Certificates, authorize distribution of a Reoffering Memorandum relating to the substitution of the letter of credit, and approve the Bond Counsel Agreement.

ANALYSIS:

SUMMARY

The District's 1996 Variable Rate Demand Certificates of Participation (1996 COPs) are secured by a letter of credit issued by Heleba Landesbank Hessen-Thuringen Girozentrale (Helaba), which was scheduled to expire on June 10, 2011. Staff

has obtained a replacement letter of credit from Union Bank, N.A., through a competitive bid process as well as a 30-day extension of the existing letter of credit to provide for an orderly substitution on or about June 30, 2011.

The 1996 COPs pay interest at a 7-day variable rate and are subject to tender on a weekly basis. A letter of credit (LOC) is required for the 1996 COPs to provide liquidity in the event of such tender, as well as credit support for the issue.

The District's continued Capital Improvement Program requires the ongoing financial funding provided by this debt while the variable rate accomplishes this at a very low cost.

The General Manager has secured the services of Suzanne Harrell, Harrell & Company Advisors, LLC as the Financial Advisor and the legal firm of Stradling, Yocca, Carlson & Rauth to serve as Bond Counsel. Both of these firms were selected due to their excellent work in the past, reasonable fees, and familiarity of the District. Due to these factors, the work can be completed in the short turnaround time required.

Certain documents are required in connection with the substitution of the letter of credit, including a Reimbursement Agreement with Union Bank and a Reoffering Memorandum describing the security for the 1996 COPs for the remarketing of the 1996 COPs on June 30, 2011. The resolutions presented to the District and the Corporation provide for approval of these documents, approval to amend the existing Installment Sale Agreement and to authorize execution of the documents.

#### BACKGROUND

The District currently has five series of outstanding debt and one loan from the State of California. Four of the debt issuances are a fixed rate, and only the 1996 COPs bear interest at a variable rate.

The 1996 COPs are issued in the par amount of \$15,400,000, of which \$11,300,000 is currently outstanding and matures in 2026. The debt was sold by the District to finance the cost of design, acquisition, and construction of certain capital improvements. The debt has a LOC for both credit enhancement and liquidity guarantee provided by Helaba. The LOC allows the interest cost to float at a variable rate, based on a short-term seven-day rate.

Recently, Heleba indicated that they are no longer interested in providing LOCs for debt of the size of the outstanding 1996 COPs as well as a desire to reduce their exposure to California debt in general. As a result, they have opted to discontinue their services as the LOC Bank. Staff has obtained a replacement letter of credit from Union Bank, N.A., through a competitive bid process as well as a 30-day extension of the Heleba letter of credit to provide for an orderly substitution on or about June 30, 2011.

Substitutions of LOC's are a common occurrence and should raise no concerns. This is a simple substitution with no substantive changes in the debt (the 1996 COPs will have the same maturity and repayment schedule). The most significant change is that Union Bank has a single "A" rating whereas Heleba had a AA rating. Staff did not receive any proposals from banks with AA ratings. This was due to the size of the issue as well as the limited number of AA banks.

The new LOC will enable the 1996 COPs to remain as variable rate debt. This action is consistent with the strategic goal to provide for sound financing of District facilities.

#### OPTIONS

When the Heleba Letter of Credit expires, instead of substituting the LOC and allowing the debt to remain outstanding, the District could consider using its existing reserves to payoff this debt. However, the District's reserves would then fall below the target levels and even below the minimum levels outlined in the Reserve Policy. This would put the District in the position of borrowing other funds at a higher cost.

With the termination of the existing LOC, the District could exercise an option to convert the debt to a fixed rate. Staff, with the assistance of Suzanne Harrell, have determined that the variable rate debt remains financially beneficial to the District. Over the remaining life of the debt, the District is expected to save approximately \$700,000 dollars by retaining the variable rate as compared to a fixed rate, taking in the cost of the LOC substitution. This analysis is required by District's debt policy relating to any conversion of variable rate debt to fixed rate debt. The variable rate debt is approximately 10% of the District's total debt portfolio, and therefore, the District's exposure to fluctuation in interest rates is minimal and manageable.

Maintaining this variable rate debt will also enhance the flexibility of the District to pay down debt as this debt can be prepaid on 30 days notice with no premium. However, based on the District's six-year rate model, the District will need to retain the debt for at least the next six years.

#### PARTIES AND COSTS

Unlike a new debt issuance, where all costs to establish the debt are paid from the proceeds of the debt issuance, on this substitution the costs will be paid from the District's reserves. The following parties are key in order to complete the LOC substitution. The list below shows the various parties and the related costs.

LOC Bank	100 basis points per year, and \$5,000 closing costs
LOC Bank Counsel	\$40,000
Financial Advisor	\$25,000 paid only if transaction is completed
Bond Counsel	\$40,000 paid only if transaction is completed, and \$2,500 closing costs
Disclosure Counsel	\$10,000 for 10(b)5 opinion required by Remarketing Agent paid only if transaction is completed
Rating Agency	\$5,000

The Financial Advisor, the Bond Counsel, and the Disclosure Counsel were selected under the General Manager's authority based on their prior work with the District and the reasonableness of their fees. This matter is time sensitive so their availability and ability to start working on this project on such short notice was a tremendous benefit to the District.

The rating agency fees are estimated above and are in line with other similar transactions.

The LOC Bank Counsel fees and the LOC Bank fee were competitively bid and were a part of the Union Bank proposal.

#### FISCAL IMPACT:

The one-time costs to substitute the LOC are expected to be approximately \$127,500. The annual LOC costs are not expected to be significantly different from the existing LOC, and will be approximately \$110,000 per year. The net result of maintaining

this variable rate debt as compared to a fixed rate borrowing is expected to save the District, after the one-time costs, approximately \$700,000 over the next fifteen years - most of which is realized during the next seven years.

STRATEGIC GOAL:

Sound financing of District facilities.

LEGAL IMPACT: \_\_\_\_\_

None.

  
\_\_\_\_\_  
General Manager

Attachments:

- A) Committee Action Form
- B) Resolution No. 4172
- C) Reoffering Memorandum
- D) First Amendment to Installment Sale Agreement
- E) Reimbursement Agreement
- F) Bond Counsel Agreement



## ATTACHMENT A

SUBJECT/PROJECT:	Substitution of the Letter of Credit for the Outstanding Variable Rate Debt
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### COMMITTEE ACTION:

The Finance, Administration and Communications Committee discussed this item at a meeting held on April 21, 2011 and the following comments were made:

- The District has five (5) outstanding debt issuances that total about \$120 million. The debt is used to fund the District's CIP Program. One (1) of the issuances is a variable rate debt which is a very low cost debt for the District and thus, the District would like to maintain it.
- It was discussed in order for the variable rate debt to be on the market, it gets remarketed every week with a new rate and the structure of the debt requires that another bank step in with a Letter of Credit (LOC) to guarantee the funds to the buyer. Without the LOC, the debt cannot be on the market.
- The current LOC is provided by Helaba and has been in place for 15 years. Helaba has indicated in the past that they are looking to limit their exposure to California debt and that the size of the District's debt is smaller than they wish to work with.
- Staff received notice from Helaba two (2) weeks ago that they will be opting out. Since receiving this notification, staff has engaged, under the General Manager's Authority, Ms. Suzanne Harrell's and a bond counsel's services. They were selected as their fees are reasonable and they have a wealth of experience with the District. The selected bond counsel worked with the District on its last two issuances and was also available to assist with short notice.
- The replacement of LOC's is fairly common and staff, knowing that Helaba may opt out, made contact with a number of banks to assure the District had options.

- An RFP was forwarded to six (6) banks and it is expected that staff will present a recommendation to the board at the May 16 Special Board meeting along with the required resolutions for both the Otay Water District and the Otay Service Corporation to adopt in order to acquire a replacement LOC for the variable debt issuance.
- Ms. Harrell indicated that the variable debt (Certificates of Participation) was issued by the District in 1996 and was secured by installment payments by the Otay Water District to the Otay Service Corporation. The agreement relates to both Otay Water District and the Otay Service Corporation and is the reason both bodies must take action.
- The District and the Otay Service Corporation will also be asked to approve the form of the Reimbursement Agreement which will delineate how the bank, providing the LOC, will be reimbursed if there is ever a draw on the LOC.
- It was noted that there will be a minor modification to the existing Trust Agreement to which the original certificates were issued to conform with the terms of the new Reimbursement Agreement. The Installment Sale Agreement will also be modified to include more contemporary language to match the 2004, 2007 and 2010 issuances.
- Staff will be requesting that the Board authorize the General Manager of the District and the Chief Financial Officer of the Service Corporation to execute all the necessary documents associated to acquire the replacement LOC.
- The RFP deadline is Monday, April 25. On April 26 the District will review the proposals received and make a selection. It was noted that the banks who were forwarded the RFP are 'AA' and 'A' credit banks. The current bank is an 'AA' credit bank. An 'A' credit bank will require that the District pay a little more interest, however, the District will look at the overall cost of the various options and select the option that would provide the least cost.
- It was discussed that the District could convert the debt to a fixed rate debt. However, after evaluating doing so, staff determined that it is still less expensive to keep it

a variable rate debt. Also, in six or seven years, the District may be in a position to pay some debt off. At that time, this variable rate debt can easily be paid off or down. It was further discussed that the variable rate debt is a small portion of the debt portfolio, so any volatility in interest rates would not have a dramatic effect on net portfolio interest expense. Staff also, per policy, reviews the District's outstanding debt periodically to determine if it would be cost effective to convert the debt to a fixed rate, pay it off, etc. The current interest rate on the variable debt is approximately 1.5%. The rate on new fixed rate debts would be approximately 5%.

The committee supported staffs' recommendation and suggested that staff present this item at the May 16, 2011 Special Board Meeting. However, the bond documents were not finalized by the May 16 board meeting and, Helaba had provided a 30-day extension on the LOC, which allowed staff to move the presentation of this item to the June 1, 2011 regularly scheduled meeting.

## RESOLUTION NO. 4172

## RESOLUTION OF THE BOARD OF DIRECTORS OF THE OTAY WATER DISTRICT APPROVING CERTAIN DOCUMENTS AND AUTHORIZING CERTAIN ACTIONS IN CONNECTION WITH A CREDIT SUBSTITUTION AND REMARKETING OF THE OTAY WATER DISTRICT VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION (1996 CAPITAL PROJECTS)

WHEREAS, the Otay Water District (the "District") and the Otay Service Corporation (the "Corporation") have previously entered into an Installment Sale Agreement dated as of June 1, 1996 (the "Installment Sale Agreement") and that certain Trust Agreement dated as of June 1, 1996 (the "Trust Agreement") by and among the District, the Corporation and the Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") pursuant to which the Otay Water District Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates") were executed and delivered; and

WHEREAS, the letter of credit securing the repayment of the Certificates under the Trust Agreement is expiring and will not be renewed; and

WHEREAS, the District desires to cause a substitute letter of credit (the "Letter of Credit") from Union Bank, N.A. (the "Bank") to be delivered to the Trustee to replace the existing letter of credit; and

WHEREAS, the substitution of the Letter of Credit from the Bank will result in a mandatory tender and remarketing of the Certificates under the terms of the Trust Agreement; and

WHEREAS, in order to effectuate the substitution of the Letter of Credit to be provided by the Bank and the remarketing of the Certificates, there has been presented to the District the forms of the following documents for approval:

- (1) A Preliminary Reoffering Memorandum;
- (2) A Reimbursement Agreement (the "Reimbursement Agreement") by and between the District and the Bank;
- (3) A First Amendment to Installment Sale Agreement (the "First Amendment to Installment Sale Agreement") by and between the District and the Corporation; and
- (4) Bond Counsel Agreement with Stradling Yocca Carlson & Rauth, a Professional Corporation.

WHEREAS, the execution and delivery of the foregoing documents are necessary to effectuate the remarketing of the Certificates which the Board of Directors has determined to be in the best interests of the District;

NOW, THEREFORE, the Board of Directors of the Otay Water District does hereby RESOLVE, DETERMINE and ORDER as follows:

Section 1. Each of the above recitals is true and correct and is adopted by the legislative body of the District.

Section 2. The forms of the First Amendment to Installment Sale Agreement and the Reimbursement Agreement (collectively, the "District Agreements") are hereby approved and each of the President of the Board of Directors, the Vice President of the Board of Directors, the Treasurer, the General Manager, the Chief Financial Officer, and their written designees (each an "Authorized Officer" and collectively the "Authorized Officers"), acting alone, is hereby authorized and directed to execute and deliver the District Agreements in the name of and on behalf of the District, in substantially the form and content now before this meeting, but with such changes, modifications, additions and deletions therein as shall be deemed necessary, desirable or appropriate by the Authorized Officer or Authorized Officers executing the same, such approval to be conclusively evidenced by the execution and delivery thereof by one or more of the Authorized Officers.

Section 3. The form of Preliminary Reoffering Memorandum presented at this meeting is hereby approved and the Remarketing Agent is hereby authorized to distribute the Preliminary Reoffering Memorandum to prospective purchasers of the Certificates in the form hereby approved, together with such additions thereto and changes therein as are determined necessary by the General Manager or the Chief Financial Officer, or their written designees, to make such Preliminary Reoffering Memorandum final as of its date for purposes of Rule 15c2-12 of the Securities and Exchange Commission, including, but not limited to, such additions and changes as are necessary to make all information set forth therein accurate and not misleading. Each of the Authorized Officers is hereby authorized to execute, approve, and deliver the final Reoffering Memorandum in the form of the Preliminary Reoffering Memorandum, together with such changes as are determined necessary by the General Manager or the Chief Financial Officer, or their written designees, to make such Reoffering Memorandum complete and accurate as of its date.

Section 4. Pursuant to Government Code Section 5922, the Board hereby determines that the Letter of Credit to be provided by the Bank and the Reimbursement Agreement are necessary and appropriate to place the obligations of the District related to the Certificates on a variable rate basis, and further determines that, the Letter of Credit is designed to reduce the total amount of interest to be paid by the District and to result in a lower cost of borrowing when used in combination with the Certificates. The Reimbursement Agreement will be executed in accordance with the provisions of Government Code Section 5922(c).

Section 5. The Authorized Officers are each authorized to execute a contract with Stradling Yocca Carlson & Rauth, a Professional Corporation, to act as Bond Counsel to the District with respect to the remarketing of the Certificates, which contract shall be in substantially the form on file with the Secretary, together with such changes as must be approved by the Authorized Officer executing the same.

Section 6. The Authorized Officers are hereby authorized and directed, to do any and all things and to execute and deliver any and all documents, including amendments to any of the existing documents and agreements relating to the Certificates, which they may deem necessary or advisable

in order to consummate the execution and delivery of the Letter of Credit and the remarketing of the Certificates and otherwise to effectuate the purposes of this resolution.

Section 7. This resolution shall take effect upon its adoption.

ADOPTED, SIGNED and APPROVED at a regular meeting of the District this 16th day of May, 2011.

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President of the Board of Directors of the Olay Water District

ATTEST:

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Secretary of the  
Board of Directors of the  
Olay Water District



DRAFT REOFFERING MEMORANDUM AS OF MAY 25, 2011

REOFFERING – NOT A NEW ISSUE – BOOK-ENTRY-ONLYRATING

Standard &amp; Poor's: \_\_\_\_\_

(See "CONCLUDING INFORMATION - Rating on the Certificate" herein)

On June 18, 1996, Best Best & Krieger LLP, Riverside, California, Special Counsel to the District, delivered their opinion in connection with the execution and delivery of the 1996 Certificates. Such opinion stated that, based upon an analysis of then existing statutes, regulations, rulings and judicial decisions, and assuming, among other matters, compliance with certain covenants and requirements, the interest component of the Installment Payments made by the District under the Installment Sale Agreement and received by the Certificate Owners was excluded from gross income for federal income tax purposes, was not an item of tax preference for purposes of federal individual or corporate alternative minimum tax, but such interest component may be included in the calculation of corporation alternative minimum taxable income. In the further opinion of Special Counsel, such interest component was exempt from State of California personal income taxes. In connection with the delivery of the Letter of Credit, Special Counsel will deliver their opinion that such delivery of the Letter of Credit will not, in and of itself, result in the inclusion of component of the Installment Payments in gross income for purposes of federal income taxation. Special Counsel has not taken and does not intend to take any action to update such opinion or to determine if the interest component of the Installment Payments is presently excluded from gross income for federal income tax purposes or exempt from State of California personal income taxes. See "LEGAL MATTERS - Tax Matters" herein.

SAN DIEGO COUNTYSTATE OF CALIFORNIA

\$11,300,000

VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION  
(1996 CAPITAL PROJECTS)

Evidencing Direct, Undivided Fractional Interests in Installment Payments to be Made by the  
OTAY WATER DISTRICT  
As Purchase Price for Certain Property Pursuant to an Installment Sale Agreement

Dated: Date of Initial Delivery

CUSIP: 688818AV5

Due: September 1, 2026

This Reoffering Memorandum amends, supplements and restates the original Official Statement dated June 17, 1996.

The Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "1996 Certificates") were originally executed and delivered pursuant to a Trust Agreement dated as of June 1, 1996, as amended (the "Trust Agreement") between the Otay Water District (the "District"), the Otay Service Corporation (the "Corporation") and the Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") and are payable from Installment Payments to be made by the District to the Corporation as payment for certain real property and improvements pursuant to an Installment Sale Agreement, as described herein and from certain funds held under the Trust Agreement and insurance or condemnation awards. The 1996 Certificates were executed and delivered to provide funds for certain storage, transmission and distribution facilities and the District's administrative headquarters.

Payment of the principal and Purchase Price of and interest component with respect to the 1996 Certificates is supported by an irrevocable, direct-pay letter of credit to be issued by Union Bank, N.A.



The Letter of Credit will permit the Trustee to draw up to an amount sufficient to pay: (i) the principal of the 1996 Certificates when due; (ii) the Purchase Price of 1996 Certificates that are purchased pursuant to tenders and that are not remarketed; and (iii) up to 34 days' interest accrued on the 1996 Certificates, all as described more completely in this Reoffering Memorandum. The Letter of Credit becomes effective on June \_\_, 2011 and expires on June \_\_, 2014, or on the earlier occurrence of certain events described in this Reoffering Memorandum. See the captions "THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT" and "THE BANK." On the fifth Business Day prior to the expiration or termination of the Letter of Credit, the 1996 Certificates will be subject to mandatory tender for purchase.

On June 30, 2011, the 1996 Certificates will be remarketed in a Weekly Rate and will continue to bear interest at a Weekly Rate unless and until the Interest Rate Period for the 1996 Certificates is converted to a different Interest Rate Period pursuant to the Trust Agreement. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS." While bearing interest in a Weekly Rate Period, interest with respect to the 1996 Certificates is payable on the first Business Day of each calendar month.

The District is required under the Installment Sale Agreement to make payments in each Fiscal Year from Taxes and from Net Revenues of the District's water system (the "Water System") in an amount sufficient to pay the annual principal and interest due with respect to the Certificates, as described herein (see "SOURCES OF PAYMENT FOR THE CERTIFICATES" and "RISK FACTORS" herein).

The 1996 Certificates are subject to optional and mandatory sinking fund prepayment and optional and mandatory tender prior to maturity as described herein. The 1996 Certificates are also subject to purchase on the demand of Owners under certain circumstances, as described in this Reoffering Memorandum. See "THE CERTIFICATES - General," "Prepayment" and "Tender and Purchase of 1996 Certificates" herein.

The 1996 Certificates were initially executed and delivered on June 18, 1996 in denominations of \$100,000 and any integral multiple thereof, and will continue as such while the 1996 Certificates bear interest in a Weekly Rate Period.

The District's obligation to make the Installment Payments is a special obligation of the District payable solely from Taxes and Net Revenues of the Water System. The obligation of the District to make the Installment Payments is an irrevocable obligation of the District payable solely from Taxes and Net Revenues but does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation other than the Taxes. The obligation of the District to make the Installment Payments under the Installment Sale Agreement does not constitute a debt of the District, the Corporation, the State of California or any political subdivision thereof in contravention of any constitutional or statutory debt limitation or restriction.

This Reoffering Memorandum describes the 1996 Certificates only while bearing interest in a Weekly Rate Period. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate with respect to the 1996 Certificates is changed to an Interest Rate Period other than the Weekly Rate Period. Rather, investors should rely upon the offering document used in connection with any such change in Interest Rate Period.

This cover page contains certain information for general reference only. It is not intended to be a summary of the security or terms of the 1996 Certificates. Investors are advised to read the entire Reoffering Memorandum to obtain information essential to making an informed investment decision.

Certain legal matters related to this Reoffering Memorandum will be passed upon by Best Best & Krieger LLP, Riverside, California, Special Counsel. Certain legal matters will be passed on for the Remarketing Agent by its counsel, \_\_\_\_\_, for the Bank by its counsel, Musick, Peeler, and Garrett, LLP and for the District and the Corporation by their counsel, Stutz, Artiano, Shinoff & Holtz, San Diego, California, and by Sirdling Vooza Carlson & Rauh, a Professional Corporation, Newport Beach, California. It is anticipated that the remarketed Certificates, in book-entry form, will be available for delivery through the facilities of The Depository Trust Company in New York, New York on or about June 30, 2011.

The date of the Reoffering Memorandum is \_\_\_\_\_, 2011

J.P. Morgan Logo

This Reoffering Memorandum and the information contained herein are subject to completion or amendment. Under no circumstances shall this Reoffering Memorandum constitute an offer to sell or a solicitation of an offer to buy nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification of the securities laws of such jurisdiction.

## GENERAL INFORMATION ABOUT THIS REOFFERING MEMORANDUM

**Use of Reoffering Memorandum.** This Reoffering Memorandum is submitted in connection with the offer and sale of the 1996 Certificates referred to herein and may not be reproduced or used, in whole or in part, for any other purpose. This Reoffering Memorandum is not to be construed as a contract with the purchasers of the 1996 Certificates.

**Estimates and Forecasts.** When used in this Reoffering Memorandum and in any continuing disclosure by the District in any press release and in any oral statement made with the approval of an authorized officer of the District or any other entity described or referenced herein, the words or phrases “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “forecast,” “expect,” “intend” and similar expressions identify “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is subject to such uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material. Such forward-looking statements include, but are not limited to, certain statements contained in the information under the caption “THE WATER SYSTEM.”

**Limit of Offering.** No dealer, broker, salesperson or other person has been authorized by the District to give any information or to make any representations in connection with the offer or sale of the Certificates other than those contained herein and if given or made, such other information or representation must not be relied upon as having been authorized by the District or the Remarketing Agent. This Reoffering Memorandum does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the 1996 Certificates by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

**Involvement of Remarketing Agent.** The Remarketing Agent has provided the following sentence for inclusion in this Reoffering Memorandum: The Remarketing Agent has reviewed the information in this Reoffering Memorandum in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Remarketing Agent does not guarantee the accuracy or completeness of such information.

**Information Subject to Change.** The information and expressions of opinions herein are subject to change without notice and neither delivery of this Reoffering Memorandum nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District or any other entity described or referenced herein since the date hereof. All summaries of the documents referred to in this Reoffering Memorandum are made subject to the provisions of such documents, respectively, and do not purport to be complete statements of any or all of such provisions.

THE CERTIFICATES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXCEPTION FROM THE REGISTRATION REQUIREMENTS CONTAINED IN SUCH ACT. THE CERTIFICATES HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE.

The CUSIP number of the 1996 Certificates is provided by Standard & Poor’s CUSIP® Service Bureau and is set forth herein for convenience of reference only. Neither the District nor the Remarketing Agent takes any responsibility for the accuracy of such number.

**OTAY WATER DISTRICT  
SAN DIEGO COUNTY, CALIFORNIA**

**BOARD OF DIRECTORS**

Jaime Bonilla, *President - Division 2*  
Gary D. Croucher, *Vice President - Division 3*  
David Gonzalez, Jr., *Treasurer - Division 1*  
Jose Lopez, *Division 4*  
Mark Robak, *Division 5*

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**MANAGEMENT TEAM**

Mark Watton, *General Manager*  
German Alvarez, *Assistant General Manager Finance & Administration*  
Manny Magaña, *Assistant General Manager Engineering & Operations*  
Joseph R. Beachem, *Chief Financial Officer*  
Rom Samo, Jr., *Chief of Administrative Services*  
Geoff Stevens, *Chief Information Officer*  
Rod Posada, *Chief of Engineering*  
Pedro Porras, *Chief of Water Operations*

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**PROFESSIONAL SERVICES**

**Special Counsel**

Best Best & Krieger LLP  
Riverside, California

**General Counsel to the District**

Stutz, Artiano, Shinoff & Holtz  
San Diego, California

**Remarketing Agent**

J.P. Morgan Securities LLC  
New York, New York

**Trustee, Tender Agent and Paying Agent**

The Bank of New York Mellon Trust Company, N.A.  
Los Angeles, California

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# REOFFERING MEMORANDUM

\$11,300,000

## VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION (1996 CAPITAL PROJECTS)

Evidencing Direct, Undivided Fractional Interests in Installment Payments to be Made by the  
OTAY WATER DISTRICT  
As Purchase Price for Certain Property Pursuant to an Installment Sale Agreement

## INTRODUCTION

*This Reoffering Memorandum dated June \_\_, 2011 amends, supplements and restates the original Official Statement dated June 17, 1996, with respect to the Variable Rate Demand Certificates of Participation (1996 Capital Projects) of the Otay Water District (the "1996 Certificates").*

*The 1996 Certificates were originally executed and delivered on June 18, 1996 in the original principal amount of \$15,400,000, of which \$11,300,000 remains outstanding.*

*This Introduction is subject in all respects to the more complete information contained and referenced elsewhere in this Reoffering Memorandum. The offering of the 1996 Certificates to potential investors is made only by means of the entire Reoffering Memorandum.*

### **Purpose**

The purpose of this Reoffering Memorandum, which includes the cover page and appendices hereto, is to set forth certain information concerning the Otay Water District, located in San Diego County, California (the "District"), in connection with \$15,400,000 aggregate principal amount of the 1996 Certificates. The 1996 Certificates evidence direct, undivided fractional interests of the registered owners thereof in Installment Payments to be made by the District, as payment for certain property pursuant to an Installment Sale Agreement dated as of June 1, 1996, as amended (the "Installment Sale Agreement") with the Otay Service Corporation (the "Corporation"). The 1996 Certificates were executed and delivered for the purposes of financing certain capital improvements of the District, and paying the costs of issuance of the 1996 Certificates. Capitalized terms used herein and not otherwise defined have the meanings ascribed to them in "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

### **The District**

The District was established in 1956. The District is a municipal water district organized and existing under and in accordance with Division 20 of the Water Code of the State of California, commencing with Section 71000, as amended (the "Law"). The District's boundaries currently encompass an area of approximately 125 square miles in San Diego County, lying immediately east of the San Diego metropolitan area and running from the City of El Cajon south to the Mexican border, abutting the cities of El Cajon and La Mesa and encompassing most of the City of Chula Vista and a small portion of the City of San Diego. The District currently serves a population of approximately 206,000 and expects the service area to experience moderate growth in the next ten years (see "OTAY WATER DISTRICT" and "APPENDIX C - ECONOMIC PROFILE FOR THE COUNTY OF SAN DIEGO" herein).

## **The Corporation**

The Corporation was organized pursuant to the Nonprofit Public Benefit Corporation Law of the State of California, being Part 2 of Division 2 of Title 1 of the California Corporations Code. It was formed for the purpose of providing financial assistance to the District by acquiring, constructing, improving and developing certain real and personal property, together with appurtenances and appurtenant work for the use, benefit and enjoyment of the public. The District's Board of Directors sits as the Corporation's Board of Directors.

## **The 1996 Certificates**

The 1996 Certificates will bear interest at the Weekly Rate, which will be computed on the basis of a year of 365 days (366 days in leap years) and the actual days elapsed and will accrue from and including the first day of each calendar month through the last day of such month (except that the initial interest period will commence on June 30, 2011). Such interest will be paid on the first Business Day of the following month, commencing August 1, 2011. When the 1996 Certificates bear interest at a Weekly Rate, interest will be determined as described under the caption "THE CERTIFICATES - Interest Rates - Weekly Rate."

The method of determining the interest rate borne by the 1996 Certificates may be changed at the option of the District in accordance with the terms of the Trust Agreement, upon notice to the Owners of the 1996 Certificates, to a Daily Rate, a Weekly Rate, a Monthly Rate, a CP Rate, or a Fixed Rate. See the caption "THE CERTIFICATES - Interest Rates."

**This Reoffering Memorandum describes the 1996 Certificates only while bearing interest at a Weekly Rate. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate period on the 1996 Certificates is changed to a period other than the Weekly Rate Period. Rather, investors should rely upon the offering document used in connection with any such change in Interest Rate Period.**

## **Security for the 1996 Certificates**

The 1996 Certificates were originally executed and delivered as variable rate certificates bearing interest in a Weekly Rate Period on June 18, 1996. On June 30, 2011 (the "Reoffering Date"), the 1996 Certificates will be remarketed in a Weekly Rate Period supported by an irrevocable direct-pay letter of credit to be issued by Union Bank, N.A. (the "Bank"). See "THE LETTER OF CREDIT AND REIMBURSEMENT AGREEMENT" herein. The 1996 Certificates presently and will continue to bear interest at a Weekly Rate unless and until the Interest Rate Period for the 1996 Certificates is converted to a different Interest Rate Period pursuant to the Trust Agreement.

The 1996 Certificates represent undivided fractional interests in the Installment Payments (the "Installment Payments") to be made by the District to the Corporation as the payment for the 1996 Project, as described herein, pursuant to a Installment Sale Agreement, dated as of June 1, 1996, between the Corporation and the District, as amended by a First Supplement to Installment Sale Agreement dated as of June 1, 2011 (as amended the "Installment Sale Agreement"). The Installment Payments are scheduled to be sufficient to pay, when due, the annual principal and interest represented by the Certificates. The Corporation has assigned to the Trustee, for the benefit of the Owners of the 1996 Certificates, the right of the Corporation to receive and collect the Installment Payments due from the District to the Corporation under the Installment Sale Agreement and other amounts payable by the District to the Corporation thereunder. For a summary of the Trust Agreement, the Installment Sale Agreement and the Reimbursement Agreement see "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS" herein. Certain capitalized terms used in this Reoffering Memorandum and not otherwise defined have the meaning given them in "APPENDIX A."

The Installment Payments are secured by a charge and lien on Taxes and Revenues of the Water System and are payable from Taxes and Net Revenues, on a parity with:

- the payments required to be made by the District under an installment purchase agreement dated as of July 1, 2004 (the “2004 Installment Purchase Agreement”) securing the District’s outstanding Revenue Refunding Certificates of Participation (1993 Water Facilities Project), Series 2004 (the “2004 Certificates”),
- the payments required to be made by the District under an installment purchase agreement dated as of March 1, 2007 (the “2007 Installment Purchase Agreement”) securing the District’s outstanding Revenue Certificates of Participation (2007 Water System Project), Series 2007 (the “2007 Certificates”), and
- the payments required to be made by the District under an installment purchase agreement dated as of March 1, 2010 (the “2010 Installment Purchase Agreement”) securing the Otay Water District Financing Authority’s outstanding Water Revenue Bonds, Series 2010A and Water Revenue Bonds, Series 2010B (collectively, the “2010 Bonds”).

See “SOURCES OF PAYMENT FOR THE CERTIFICATES - Installment Payments” herein.

Collectively, the 2004 Certificates, the 2007 Certificates and the 2010 Bonds are referred to herein as the “Existing Parity Obligations.” See “THE WATER SYSTEM - Outstanding Indebtedness of the District” herein.

**The District’s obligation to make the Installment Payments is a special obligation of the District payable solely from Taxes and Net Revenues of the Water System. The obligation of the District to make the Installment Payments is an irrevocable obligation of the District payable solely from Taxes and Net Revenues but does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation other than the Taxes. The obligation of the District to make the Installment Payments under the Installment Sale Agreement does not constitute a debt of the District, the Corporation, the State of California or any political subdivision thereof in contravention of any constitutional or statutory debt limitation or restriction.**

## **Letter of Credit**

On June 30, 2011, an irrevocable direct-pay letter of credit, dated June 30, 2011 (the “Letter of Credit”), provided by Union Bank, N.A. (the “Bank”), is expected to replace the existing irrevocable, direct-pay letter of credit issued by Heleba Landesbank Hessen-Thüringen Girozentrale, to support the payment of the principal and Purchase Price of, and interest on, the 1996 Certificates. The Letter of Credit will be issued pursuant to a Reimbursement Agreement, dated as of June 30, 2011 (the “Reimbursement Agreement”), to be entered into by and between the District and the Bank. The Letter of Credit will expire on June \_\_, 2014, or on the earlier occurrence of certain events as described herein. The initial Letter of Credit may be replaced with another credit facility as described under the caption “THE LETTER OF CREDIT AND REIMBURSEMENT AGREEMENT.” The initial Letter of Credit, or any qualified replacement or extension, issued by the Bank, or any other financial institution, is called a “Letter of Credit.” Any financial institution which at the time is the issuer of a Letter of Credit is called the “Bank.”

The initial Letter of Credit will be issued in the total amount of \$11,426,313, which is equal to: (i) the outstanding aggregate principal amount of the 1996 Certificates (\$11,300,000); plus (ii) 34 days’ interest thereon at an annual rate of 12% (\$126,313).

## **No Continuing Disclosure**

The 1996 Certificates are exempt from the rules of the Securities and Exchange Commission relating to continuing disclosure of annual financial information and certain material events. However, the District provides continuing disclosure of annual financial information and certain material events with respect to the Existing Parity Obligations.

## **Information Concerning this Reoffering Memorandum**

This Reoffering Memorandum speaks only as of its date. The information set forth herein has been obtained by the District from sources which are believed to be accurate and complete, but such information is not guaranteed as to accuracy or completeness, nor has it been independently verified and is not to be construed as a representation by the District or the Remarketing Agent. Statements contained in this Reoffering Memorandum which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended as such and are not to be construed as representations of fact.

**Availability of Legal Documents.** The summaries and references contained herein with respect to the Trust Agreement, the Installment Sale Agreement, the Reimbursement Agreement, the Certificates and other statutes or documents do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute, and references to the 1996 Certificates are qualified in their entirety by reference to the form thereof included in the Trust Agreement. Definitions of certain terms used herein are set forth in "APPENDIX A" hereto. Copies of these documents may be obtained at the corporate trust office of the Trustee, The Bank of New York Mellon Trust Company, N.A., Los Angeles, California or from the District, 2554 Sweetwater Springs Blvd., Spring Valley, California 91978.

# **THE CERTIFICATES**

## **General**

**This Reoffering Memorandum describes the 1996 Certificates only while bearing interest at a Weekly Rate. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate period on the 1996 Certificates is changed to a period other than the Weekly Rate Period. Rather, investors should rely upon the offering document used in connection with any such change in Interest Rate Period.**

The 1996 Certificates were initially executed and delivered in the aggregate principal amount of \$15,400,000, of which \$11,300,000 remains outstanding. The 1996 Certificates are dated the date of initial delivery of the 1996 Certificates, and will bear interest at a Weekly Rate, until converted to another interest rate Mode as described herein. The 1996 Certificates will mature, subject to prior redemption, on September 1, 2026. Interest with respect to the 1996 Certificates bearing interest at the Weekly Rate accruing during any month will be payable on the first Business Day of the following month. Interest with respect to the 1996 Certificates is also payable on any Mandatory Purchase Date. Interest will be determined as described herein. While bearing interest at the Weekly Rate, the 1996 Certificates will be issued in Authorized Denominations of \$100,000 and any integral multiple thereof.

The term "Business Day" is defined in the Trust Agreement to mean any day of the year other than Saturday or Sunday on which banks in New York, New York, and in Los Angeles, California, or any other city in which the principal office of the Bank may be located are not authorized or required by law or executive order to close and on which the New York Stock Exchange is not closed. If the date for making any payment on the 1996 Certificates is not a Business Day, the payment will be made on the next Business Day with the same effect as if made on the nominal date and no interest will accrue between the nominal date and the actual payment date.

The 1996 Certificates will be registered in the name of Cede & Co., as registered owner and nominee of The Depository Trust Company, New York, New York (“DTC”). So long as DTC, or its nominee Cede & Co., is the registered owner of all the 1996 Certificates, all payments of principal of and interest with respect to the 1996 Certificates and the Purchase Price of the 1996 Certificates will be made directly to DTC. Disbursement of such payments to the DTC Participants (as defined below) will be the responsibility of DTC. Disbursement of such payments to the Beneficial Owners (as defined below) of the 1996 Certificates will be the responsibility of the DTC Participants as more fully described herein. See the caption “Book-Entry Only System” below and “APPENDIX E - DTC AND THE BOOK-ENTRY-ONLY SYSTEM.”

*There are a number of provisions in the Trust Agreement relating to the terms of Bank Certificates (i.e., 1996 Certificates purchased by the Bank pursuant to the Letter of Credit and Reimbursement Agreement) that are not described in this Reoffering Memorandum. All references to the terms of the 1996 Certificates in this Reoffering Memorandum describe only 1996 Certificates that are not owned by the Bank unless expressly indicated herein.*

## **Interest Rates**

**General.** The method of determining the interest rate borne by the 1996 Certificates may be changed at the option of the District in accordance with the terms of the Trust Agreement, upon notice to the Owners of the 1996 Certificates, to a Daily Rate, a Weekly Rate, a Monthly Rate (collectively, the “Variable Rates”), a CP Rate, or a Fixed Rate.

The Variable Rate is required to be the lowest rate of interest which, in the judgment of the Remarketing Agent, would cause the 1996 Certificates to have a market value equal to the principal amount thereof, plus accrued interest, under prevailing market conditions as of the date of determination of the Variable Rate. In no event may the Variable Rate for any Variable Rate Period exceed 12% (the “Maximum Rate”).

All determinations of Variable Rates pursuant to the Trust Agreement are conclusive and binding upon the District, the Corporation, the Trustee, the Tender Agent, the Bank and the Owners of the 1996 Certificates.

**Weekly Rate.** Commencing June 30, 2011, the 1996 Certificates will bear interest at the Weekly Rate, which will be computed on the basis of a year of 365 days (366 days in leap years) and the actual days elapsed and will accrue from and including the first day of each calendar month through the last day of such month (except that the initial interest period will commence on June 30, 2011). Such interest will be paid on the first Business Day of the following month, commencing August 1, 2011.

The Weekly Rate for each Weekly Rate Period is required to be determined by the Remarketing Agent not later than 4:30 p.m. (New York City time) on each Tuesday or, if such Tuesday is not a Business Day, the last Business Day immediately prior to the commencement date of the Weekly Rate Period to which it relates. Weekly Rate Periods extend from Wednesday of each week to but excluding Wednesday of the following week except that in the case of a conversion to a Weekly Rate Period from a different Variable Rate Period or from CP Rate Periods, the initial Weekly Rate Period for the 1996 Certificates will extend from the Weekly Rate Conversion Date to Wednesday of the following week; in the case of a conversion of 1996 Certificates from a Weekly Rate Period to a different Rate Period, the last Weekly Rate Period will end on the Conversion Date; and, in the case of the first Weekly Rate Period, which shall commence on the Date of Delivery of the 1996 Certificates and extend to Wednesday of the following week.

## **Conversion Between Variable Rate Periods and CP Rate Periods**

At the option of the District, subject to certain conditions, and upon proper notice to the Trustee, the 1996 Certificates may be converted from one Variable Rate Period to another Variable Rate Period or to or from CP Rate Periods in accordance with the provisions therefor in the Trust Agreement.

Upon a conversion of 1996 Certificates to or from one Variable Rate Period to another Variable Rate Period or to or from CP Rate Periods, such 1996 Certificates will be subject to a mandatory tender, and the Owners of such 1996 Certificates may not elect to retain their 1996 Certificates.

In the case of conversion between Variable Rate Periods or to CP Rate Periods, the Conversion Date is required to be an Interest Payment Date for the Variable Rate Period from which the conversion is to be made. In the case of conversion from CP Rate Periods, the Conversion Date is required to be both (1) the first Business Day of a calendar month and (2) the last Interest Payment Date on which interest is payable for any CP Rate Periods previously established for any 1996 Certificate pursuant to the Trust Agreement.

Not less than 30 days nor more than 60 days prior to the Conversion Date, the Trustee is required to mail or cause the Trustee to mail a written notice of the conversion to the Bank, the District and all of the Owners of the 1996 Certificates.

Notwithstanding the delivery of notice of conversion pursuant to the Trust Agreement conversion to a new Rate Period will not take effect if:

- (1) The Remarketing Agent fails to determine a Variable Rate or CP Rate for the Rate Period to which the conversion is to be made;
- (2) Any notice of conversion required by the Trust Agreement is not given when required;
- (3) There is not delivered to the District, the Remarketing Agent and the Trustee an Opinion of Special Counsel dated as of the Conversion Date; or
- (4) Such notice of conversion is rescinded by the District by written notice to the Trustee and the Remarketing Agent delivered prior to the applicable Conversion Date. If the Trustee receives notice of such rescission prior to the time the Trustee has given notice to the Owners of the 1996 Certificates, then such notice of conversion will be of no force and effect. If the Trustee receives notice of such rescission after the Trustee has given notice to the Owners of the 1996 Certificates, then the Certificates will automatically adjust to the Weekly Rate Period. Any purchases of 1996 Certificates scheduled or required to take place on the proposed effective date of any Rate Period will take place on such date. Any election to retain 1996 Certificates which are subject to mandatory tender, received by the Trustee pursuant to the Trust Agreement will be of no force and effect and the Trustee will immediately give written notice thereof to such Owners. No Opinion of Special Counsel is required in connection with any automatic adjustment to a Weekly Rate Period pursuant to such provision in the Trust Agreement.

Except as provided in (4) above, in any such event, the 1996 Certificates which were to be converted will automatically be converted to a Weekly Rate Period on the date such conversion was to be made, but any mandatory or optional tender for purchase on the Conversion Date will be carried out. No cancellation of a conversion will constitute an Event of Default under the Trust Agreement. Upon the occurrence of any event described in (1) above, the Weekly Rate will be the per annum rate of interest determined on each Tuesday (or if such day is not a Business Day, the next prior Business Day) by the Trustee which is 80% of the certificate equivalent yield for 30-day United States Treasury Bills sold at the last United States Treasury auction occurring prior to such day, which yield shall be calculated in accordance with standard practices in the banking industry on the basis of the discount rates at which such bills were sold but not to exceed the Maximum Rate.

## **Conversion to Fixed Rates**

The 1996 Certificates, in whole but not in part, will be converted to represent interest calculated at Fixed Rates upon the District's request. Upon a conversion of 1996 Certificates to represent interest calculated at Fixed Rates, such 1996 Certificates will be subject to mandatory tender, and the Owners of such 1996 Certificates may not elect to retain their 1996 Certificates. As a condition of any Fixed Rate conversion, the Trustee, the Bank and the Remarketing Agent must receive an Opinion of Special Counsel. The Fixed Rate Conversion Date will be (1) in the case of a conversion from a Variable Rate Period, an Interest Payment Date for the 1996 Certificates for the Variable Rate Period from which the conversion is to be made, and (2) in the case of a conversion from CP Rate Periods, a day which is both (A) the first Business Day of a calendar month and (B) the last Interest Payment Date for the 1996 Certificates on which interest is payable for any and all CP Rate Periods theretofore established for the 1996 Certificates pursuant to the Trust Agreement.

The Fixed Rate is required to be the lowest rate (not in excess of the maximum rate of interest allowed by law) which, in the judgment of the Remarketing Agent, as of the date of determination and under prevailing market conditions, would cause the 1996 Certificates of such maturities to have a market value equal to the principal amount thereof, plus accrued interest.

The Trustee is required to mail or cause the Trustee to mail a notice of the proposed conversion to the Owners of all 1996 Certificates to be converted not less than 30 days nor more than 60 days prior to the proposed Fixed Rate Conversion Date and state that (1) the 1996 Certificates are subject to mandatory tender for purchase with no right to retain on the Fixed Rate Conversion Date at a Purchase Price of par plus accrued interest; and (2) on and after the Fixed Rate Conversion Date the Certificate's shall be deemed purchased on that date, and thereafter the Owner will have no further rights under the Trust Agreement except to receive the Purchase Price.

Notwithstanding the delivery of notice of a Fixed Rate conversion pursuant to the Trust Agreement, conversion of the 1996 Certificates to a Fixed Rate Period will not take effect if (1) the District withdraws such notice of conversion not later than the Business Day preceding the date on which the Fixed Rate is to be determined; (2) the Remarketing Agent fails to determine a Fixed Rate; (3) any notice required by the Trust Agreement is not given when required; or (4) upon conversion any Fixed Rate 1996 Certificates would be Bank 1996 Certificates unless the Bank consents. In any of such events, the 1996 Certificates will automatically be converted to a Weekly Rate for a Weekly Rate Period which will commence on the date the Fixed Rate conversion was to be made, but the mandatory tender for purchase will still be carried out if notice of the Fixed Rate conversion had been given to the Owners. Withdrawal of a conversion notice must be given by the District to the Trustee, the Tender Agent, the Remarketing Agent and the Bank, by telephone, promptly confirmed in writing. No cancellation of a Fixed Rate conversion pursuant to this paragraph constitutes an Event of Default under the Trust Agreement. If the 1996 Certificates are converted to represent interest calculated at a Weekly Rate rather than a Fixed Rate, and the Remarketing Agent fails to set a Weekly Rate, the Weekly Rate shall be the per annum rate of interest determined on each Tuesday (or if such day is not a Business Day, the immediately preceding Business Day) by the Trustee which is 80% of the certificate equivalent yield for 30-day United States Treasury Bills sold at the last United States Treasury auction occurring prior to such day, which yield shall be calculated in accordance with standard practices in the banking industry on the basis of the discount rate at which such bills were sold but will not exceed the Maximum Rate.

Following the Fixed Rate Conversion Date, the 1996 Certificates will no longer be secured by the Letter of Credit and will no longer be subject to tender for purchase.

## Tender and Purchase of 1996 Certificates

### Tenders During Variable Rate Periods

During any Variable Rate Period with respect to the 1996 Certificates, the Owners of 1996 Certificates (other than Bank 1996 Certificates) may elect to have their 1996 Certificates (or portions thereof in Authorized Denominations) purchased at the Purchase Price as set forth below:

- 1996 Certificates representing interest at Daily Rates may be tendered for purchase on any Business Day upon telephonic notice of tender given (promptly confirmed in writing) to the Tender Agent not later than 11:00 a.m. (New York City time) on the Purchase Date.
- 1996 Certificates representing interest at Weekly Rates may be tendered for purchase on any Business Day upon telephonic notice of tender (promptly confirmed in writing) to the Tender Agent not later than 5:00 p.m. (New York City time) on a Business Day not less than seven days prior to the Purchase Date.
- 1996 Certificates representing interest at Monthly Rates may be tendered for purchase on any Interest Payment Date upon delivery of a written notice of tender to the Tender Agent not later than 4:00 p.m. (New York City time) on a Business Day that is not less than 7 days prior to the Purchase Date.

Each notice of tender must, in the case of a written notice, be delivered to the Tender Agent at the address below, and must be satisfactory to the Tender Agent. Such notice of tender must also state, whether delivered in writing or by telephone, promptly confirmed in writing, the principal amount of the 1996 Certificate or portion thereof, that the Owner irrevocably demands purchase of such 1996 Certificate or portion thereof, the date on which such 1996 Certificate or portion thereof is to be purchased and payment instructions. Such notice of tender will automatically constitute, whether delivered in writing or by telephone, (A) an irrevocable offer to sell the 1996 Certificates (or portion thereof) to which the notice relates on the Purchase Date to any purchaser selected by the Remarketing Agent at the Purchase Price, (B) an irrevocable authorization and instruction to the Trustee to effect transfer of such 1996 Certificates (or portion thereof), upon payment of such price to the Trustee on the Purchase Date, (c) an irrevocable authorization and instruction to the Tender Agent to effect the exchange of the 1996 Certificates to be purchased in whole or in part for other 1996 Certificates in an equal aggregate principal amount so as to facilitate the sale of such 1996 Certificates (or portion thereof), and (D) an acknowledgment that such Owner will have no further rights with respect to such 1996 Certificates (or portion thereof) upon payment of the Purchase Price thereof by the Trustee on the Purchase Date, except for the right of such Owner to receive such Purchase Price upon surrender of such 1996 Certificates to the Tender Agent. The determination of the Tender Agent as to whether a notice of tender has been properly delivered pursuant to the foregoing will be conclusive and binding upon the Owner.

Notices in respect of optional tenders must be delivered to the Tender Agent as follows:

#### First Class/Registered/Certified

The Bank of New York Mellon Trust Company,  
N.A.  
Global Corporate Trust  
P.O. Box 396  
East Syracuse, NY 13057  
Telephone: (800) 254-2826

#### Express Delivery Only

The Bank of New York Mellon Trust Company,  
N.A.  
Global Corporate Trust  
111 Sanders Creek Parkway  
East Syracuse, NY 13057  
Telephone: (800) 254-2826

### **Mandatory Tenders Upon Conversion**

In the case of any conversion from one Variable Rate Period to another Variable Rate Period or to a CP Rate Period, the 1996 Certificates to be converted are subject to mandatory tender for purchase on the Conversion Date at the Purchase Price.

### **Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit**

Prior to the Fixed Rate Conversion Date of the 1996 Certificates, the 1996 Certificates are subject to mandatory tender for purchase without the right to retain at the Purchase Price on a Business Day that is at least five days prior to the date on which the Letter of Credit is to be cancelled in connection with replacement by a Substitute Facility pursuant to the Trust Agreement. The 1996 Certificates are also subject to mandatory tender for purchase without the right to retain at the Purchase Price on a Business Day which is at least five days prior to a termination or expiration of the Letter of Credit. In either event, the Owners of the 1996 Certificates may not elect to retain their 1996 Certificates.

Notice of mandatory tender is required to be given by mail by the Registrar at the direction of the Trustee to the Bank and the Owners of such 1996 Certificates by first class mail not less than 15 nor more than 60 days prior to the mandatory tender date.

### **Purchase of Tendered 1996 Certificates**

Before 4:00 p.m. (New York City time) on the Purchase Date and upon receipt by the Trustee of 100% of the aggregate Purchase Price of the tendered 1996 Certificates, the Trustee is required to pay the Purchase Price of such 1996 Certificates to the Owners thereof at its principal office or by bank wire transfer. Payments are required to be made in immediately available funds. All 1996 Certificates to be purchased on any date are required to be delivered to the principal corporate trust office of the Tender Agent at or before 11:30 a.m. (New York City time) on the Purchase Date.

If the Owner of any 1996 Certificates (or portion thereof) that is subject to purchase pursuant to the Trust Agreement fails to surrender such 1996 Certificates to the Tender Agent for purchase on the Purchase Date, and if the Tender Agent is in receipt of the Purchase Price therefor, such 1996 Certificates (or portion thereof) will nevertheless be deemed purchased on the Purchase Date and ownership of such 1996 Certificates (or portion thereof) will be transferred to the purchaser thereof as provided in the Trust Agreement. Any Owner who fails to deliver a 1996 Certificate for purchase as required above will have no further rights thereunder except the right to receive the Purchase Price thereof upon presentation and surrender of said 1996 Certificate to the Tender Agent.

### **Insufficient Funds for Purchases**

If as a result of a default by the Bank under the terms of the Letter of Credit the moneys available for purchase of 1996 Certificates pursuant to the Trust Agreement are inadequate for the purchase of all 1996 Certificates that are tendered on any Purchase Date, all 1996 Certificates will continue to represent interest at the same rate as in effect on the day prior to the Purchase Date to the date on which the earliest of the following occurs: (i) the Fixed Rate Conversion Date for the 1996 Certificates, (ii) the date on which any default by the Bank under the terms of the Letter of Credit has been cured, or (iii) the date on which a Substitute Facility meeting the requirements of the Trust Agreement has been obtained. If there are insufficient funds for purchase, the Trustee is required immediately (but no later than the end of the next succeeding Business Day) to return all tendered 1996 Certificates to the Owners thereof, return all moneys received from the purchase of such 1996 Certificates to the persons who provided such moneys and notify all Owners of the 1996 Certificates and the Bank in writing of the interest rate to be effective.

## **Tender of 1996 Certificates in Book-Entry System Are Subject to DTC Procedures**

As long as the book-entry system is in effect with respect to the 1996 Certificates, all tenders for purchase and deliveries of 1996 Certificates optionally tendered for purchase upon election of the Owner or subject to mandatory tender under the provisions of the Trust Agreement will be made pursuant to DTC's procedures as in effect from time to time, and none of the District, the Trustee or the Remarketing Agent have any responsibility for or liability with respect to the implementation of such procedures. For a description of the tender procedures through DTC, see "APPENDIX E - DTC AND THE BOOK-ENTRY-ONLY SYSTEM."

## **Prepayment**

### **Optional Prepayment**

While the 1996 Certificates bear interest at a Weekly Interest Rate, the 1996 Certificates are subject to prepayment at the option of the District, in whole or in part on any Interest Payment Date at a prepayment price of 100% of the principal amount thereof.

### **Mandatory Prepayment**

***Mandatory Sinking Fund Prepayment.*** The 1996 Certificates are subject to mandatory sinking fund prepayment on September 1 in each year on or after September 1, 2011 by lot, at a prepayment price equal to the principal amount thereof, without premium, together with accrued interest to the date of prepayment, from the principal component of the Installment Payment to be paid by the District pursuant to the Installment Sale Agreement with respect to each such prepayment date as follows:

<u>Prepayment Date (September 1)</u>	<u>Principal Amount of 1996 Certificates To Be Prepaid</u>
2011	\$ 400,000
2012	500,000
2013	500,000
2014	500,000
2015	600,000
2016	600,000
2017	600,000
2018	700,000
2019	700,000
2020	700,000
2021	800,000
2022	800,000
2023	900,000
2024	900,000
2025	1,000,000
2026 (maturity)	1,100,000

If some but not all of the 1996 Certificates have been otherwise prepaid, the total principal amount of 1996 Certificates to be prepaid pursuant to a mandatory sinking fund prepayment subsequent to such other prepayment shall be reduced to correspond to the principal components of the Installment Payments scheduled to be paid in each year thereafter pursuant to the Installment Sale Agreement. If the sinking

fund prepayment amounts of the final maturity of the 1996 Certificates are converted to serial maturities, then such 1996 Certificates shall not be subject to mandatory sinking fund prepayment.

***Prepayment From Net Proceeds of Insurance and Condemnation.*** The 1996 Certificates are subject to mandatory prepayment on the earliest practicable date for which notice of prepayment may be given, from net proceeds of insurance or condemnation of the 1996 Project (including the proceeds of any self-insurance), as a whole or in part, in any integral multiple of an authorized denomination, at a prepayment price equal to the principal amount thereof, together with accrued interest to the date fixed for prepayment, without premium. Any surplus net proceeds not equal to an authorized denomination shall be deposited in the Principal Account of the Certificate Payment Fund.

### **General Prepayment Provisions**

***Selection of 1996 Certificates for Prepayment.*** The 1996 Certificates shall be prepaid in the following order of priority (and, subject to the foregoing, by lot within each priority):

First, any Bank Certificates;

Second, any 1996 Certificates which have been tendered to the Tender Agent on the date fixed for prepayment, the notice of which tender shall have been given to the Trustee prior to the selection of 1996 Certificates for such prepayment pursuant to the Trust Agreement; and

Third, the Outstanding 1996 Certificates not previously called for prepayment.

***Notice of Prepayment.*** When prepayment is authorized or required pursuant to the Trust Agreement, the Trustee shall give notice of the prepayment of the 1996 Certificates. Such notice shall specify: (a) that the 1996 Certificates or a designated portion thereof are to be prepaid, (b) the date of prepayment, and (c) the place or places where the prepayment will be made. Such notice shall further state that on the specified date there shall become due and payable upon each Certificate, the principal, together with interest accrued to said date, and that from and after such date interest with respect thereto shall cease to accrue and be payable.

Notice of the prepayment of 1996 Certificates, other than mandatory sinking fund prepayment and excepting any notice that refers to 1996 Certificates that are the subject of an advance refunding, shall be circulated only if sufficient funds have been deposited with the Trustee to pay the prepayment price of the 1996 Certificates to be prepaid.

Notice of such prepayment shall be mailed first class postage prepaid to the Remarketing Agent and Securities Depositories and the respective Owners designated for prepayment at their addresses appearing on the Certificate registration books at least thirty (30) days but not more than sixty (60) days (five days with respect to optional prepayment of 1996 Certificates prior to the prepayment date), which notice shall, in addition to setting forth the above information, set forth, in the case of each Certificate called only in part, the portion of the principal thereof which is to be prepaid.

Neither failure to receive such notice nor any immaterial defect in any notice so mailed shall affect the sufficiency of the proceedings for the prepayment of such 1996 Certificates.

***Partial Prepayment of Certificate.*** Upon surrender of any Certificate prepaid in part only, the Trustee shall execute and deliver to the Owners, at the expense of the District, a new Certificate or 1996 Certificates of authorized denominations equal in aggregate principal amount to the unprepaid portion of the Certificate surrendered and of the same interest rate and the same maturity. Such partial prepayment shall be valid upon payment of the amount thereby required to be paid to such Owner, and the District, the Corporation and the Trustee shall be released and discharged from all liability to the extent of such payment.

***Effect of Notice of Prepayment.*** Notice having been given as aforesaid, and the moneys for the prepayment (including the interest to the applicable date of prepayment), having been set aside in the Certificate Payment Fund, the 1996 Certificates called for prepayment shall become due and payable on said date of prepayment, and, upon presentation and surrender thereof at the office or offices specified in said notice, said 1996 Certificates shall be paid at the unpaid principal amount with respect thereto, plus premium, if any, and interest accrued and unpaid to said date of prepayment.

If, on said date of prepayment, moneys for the prepayment of all the 1996 Certificates to be prepaid, together with interest to said date of prepayment, shall be held by the Trustee so as to be available therefor on said date of prepayment, and if notice of prepayment thereof shall have been given as aforesaid, then, from and after said date of prepayment, interest with respect to the 1996 Certificates called for prepayment shall cease to accrue and become payable. All moneys held by or on behalf of the Trustee for the prepayment of 1996 Certificates shall be held in trust for the account of the Owners so to be prepaid.

## **SPECIAL CONSIDERATIONS RELATING TO THE 1996 CERTIFICATES SUBJECT TO OPTIONAL TENDER AND REMARKETING**

### **The Remarketing Agent is Paid by the District**

The Remarketing Agent's responsibilities include determining the interest rate from time to time and remarketing 1996 Certificates that are optionally or mandatorily tendered by the owners thereof (subject, in each case, to the terms of the Remarketing Agreement), as further described in this Reoffering Memorandum. The Remarketing Agent is appointed by the District and is paid by the District for its services. As a result, the interests of the Remarketing Agent may differ from those of existing holders and potential purchasers of 1996 Certificates.

### **The Remarketing Agent Routinely Purchases 1996 Certificates for Its Own Account**

The Remarketing Agent acts as remarketing agent for a variety of variable rate demand obligations and, in its sole discretion, routinely purchases such obligations for its own account. The Remarketing Agent is permitted, but not obligated, to purchase tendered 1996 Certificates for its own account and, in its sole discretion, routinely acquires such tendered 1996 Certificates in order to achieve a successful remarketing of the 1996 Certificates (i.e., because there otherwise are not enough buyers to purchase the 1996 Certificates) or for other reasons. However, the Remarketing Agent is not obligated to purchase 1996 Certificates, and may cease doing so at any time without notice. The Remarketing Agent may also make a market in the 1996 Certificates by routinely purchasing and selling 1996 Certificates other than in connection with an optional or mandatory tender and remarketing. Such purchases and sales may be at or below par. However, the Remarketing Agent is not required to make a market in the 1996 Certificates. The Remarketing Agent may also sell any 1996 Certificates it has purchased to one or more affiliated investment vehicles for collective ownership or enter into derivative arrangements with affiliates or others in order to reduce its exposure to the 1996 Certificates. The purchase of 1996 Certificates by the Remarketing Agent may create the appearance that there is greater third party demand for the 1996 Certificates in the market than is actually the case. The practices described above also may result in fewer 1996 Certificates being tendered in a remarketing.

## 1996 Certificates May Be Offered at Different Prices on Any Date Including a Rate Determination Date

Pursuant to the Remarketing Agreement, the Remarketing Agent is required to determine the applicable rate of interest that, in its judgment, is the lowest rate that would permit the sale of the 1996 Certificates bearing interest at the applicable interest rate at par plus accrued interest, if any, on and as of the commencement of the applicable Weekly Rate Period. The interest rate will reflect, among other factors, the level of market demand for the 1996 Certificates (including whether the Remarketing Agent is willing to purchase 1996 Certificates for its own account). There may or may not be 1996 Certificates tendered and remarketed on the commencement of the applicable Weekly Rate Period, the Remarketing Agent may or may not be able to remarket any 1996 Certificates tendered for purchase on such date at par and the Remarketing Agent may sell 1996 Certificates at varying prices to different investors on such date or any other date. The Remarketing Agent is not obligated to advise purchasers in a remarketing if it does not have third party buyers for all of the 1996 Certificates at the remarketing price. In the event that the Remarketing Agent owns any 1996 Certificates for its own account, it may, in its sole discretion in a secondary market transaction outside the tender process, offer such 1996 Certificates on any date, including the date of the commencement of the applicable Weekly Rate Period, at a discount to par to some investors.

## The Ability to Sell the 1996 Certificates Other Than through Tender Process May Be Limited

The Remarketing Agent may buy and sell 1996 Certificates other than through the tender process. However, it is not obligated to do so and may cease doing so at any time without notice and may require holders that wish to tender their 1996 Certificates to do so through the Tender Agent with appropriate notice. Thus, investors who purchase the 1996 Certificates, whether in a remarketing or otherwise, should not assume that they will be able to sell their 1996 Certificates other than by tendering the 1996 Certificates in accordance with the tender process.

## SOURCES AND USES OF FUNDS

The sources and uses of funds with respect to initial delivery of the 1996 Certificates were as follows:

### *Sources*

Principal Amount of 1996 Certificates	<u>\$15,400,000</u>
Total	<u>\$15,400,000</u>

### *Uses*

Deposit to Acquisition Fund	\$15,192,645
Underwriter's Discount	22,355
Costs of Issuance <sup>(1)</sup>	<u>185,000</u>
Total	<u>\$15,400,000</u>

<sup>(1)</sup> Included legal, financing and consulting fees, fees associated with the letter of credit, rating agency fees, printing costs and other miscellaneous expenses.

## **Letter of Credit**

On June 30, 2011, the Letter of Credit is expected to be replaced the existing irrevocable, direct-pay letter of credit dated issued by Landesbank Hessen-Thüringen Girozentrale (Helaba). The Letter of Credit is issued for the benefit of the 1996 Certificates to provide the payment of principal and Purchase Price of, and interest with respect to, the 1996 Certificates as described under the caption "THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT." Prior to the expiration date of the Letter of Credit, the 1996 Certificates will be subject to mandatory purchase. See the caption "THE CERTIFICATES - Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit."

## **Alternate Letter of Credit**

The Trust Agreement provides that if at any time there has been delivered to the Trustee: (i) a Substitute Facility in substitution for the Letter of Credit then in effect; (ii) an opinion of counsel stating that the delivery of such Substitute Facility to the Trustee is authorized under the Trust Agreement and complies with the terms thereof; (iii) ) an Opinion of Bond Counsel that the proposed substitution will not adversely affect the exclusion of interest on the 1996 Certificates from gross income for federal income tax purposes; (iv) one or more opinions of counsel addressed to the Trustee, to the effect, singly or together, that: (A) the Substitute Facility is a legal, valid and binding obligation of the obligor, enforceable against the obligor in accordance with its terms, except as limited by applicable reorganization, insolvency, liquidation, readjustment of debt, moratorium or other similar laws affecting the enforcement of the rights of creditors generally as such laws may be applied in the event of a reorganization, insolvency, liquidation, readjustment of debt or other similar proceeding of or moratorium applicable to the obligor and by general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law); and (B) payments made by the obligor under the Substitute Facility will not be voidable under Section 547 of the United States Bankruptcy Code in the context of a case or proceeding by or against the District or any Affiliates thereof under the United States Bankruptcy Code; (v) if a rating or ratings on the Certificates shall be in effect on the date of such substitution, written evidence from Moody's and/or Standard & Poor's, as applicable, to the effect that such rating agency has reviewed the proposed Substitute Facility and that the substitution of the proposed Substitute Facility for the existing Facility will not, by itself, result in a reduction or withdrawal of its rating on the Certificates; and (vi) written evidence that notice of such proposed substitution has been sent to the Owners prior to such substitution, then the Trustee shall, so long as such Substitute Facility shall contain administrative procedures which are acceptable to the Trustee in its reasonable discretion, accept such Substitute Facility and promptly surrender the existing Facility to the issuer thereof, and surrender the Letter of Credit then in effect to the Bank. The 1996 Certificates will be subject to mandatory tender for purchase on the substitution date. See the caption "THE CERTIFICATES - Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit."

## **THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT**

*The following information has been provided by the Bank for use in this Reoffering Memorandum. Such information has not been confirmed or verified by the District or the Remarketing Agent. Neither the District nor the Remarketing Agent make any representation as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof. Further, no representation is made herein that the information contained or incorporated herein by reference is correct as of any time subsequent to the date hereof.*

The Irrevocable Letter of Credit (the "Letter of Credit") will be issued by the Bank pursuant to the Reimbursement Agreement dated as of June 30, 2011 (the "Reimbursement Agreement"), by and between the District and the Bank. The following summarizes certain provisions of the Letter of Credit and the Reimbursement Agreement, to which documents reference is made for the complete provisions thereof.

The provisions of any substitute letter of credit and related reimbursement agreement may be different from those summarized below.

## **Letter of Credit**

(to be conformed when draft LOC is received)

The 1996 Certificates are secured by the Letter of Credit issued by the Bank pursuant to the Reimbursement Agreement. The Letter of Credit will expire on the date that is the earliest of (a) June 30, 2014, provided however, the District may request the Bank to extend the Letter of Credit by making such a request not less than six months prior to the expiration date, but extension of the expiration date of the Letter of Credit is solely at the Bank's discretion; (b) the date on which the Bank honors a payment on the Letter of Credit in connection with the purchase or redemption of all of the Bonds, the conversion of the interest rate on the Bonds or a final payment with respect to the Bonds; (c) fifteen (15) days after receipt by the Trustee of written notice from the Bank directing the Trustee to purchase or redeem all outstanding Bonds and present a final drawing under the Letter of Credit as a result of the occurrence of an Event of Default under the Reimbursement Agreement; or (d) the date on which the Letter of Credit is surrendered by the Trustee to the Bank.

While in effect, the Letter of Credit entitles the Trustee to draw on the Letter of Credit, on such dates and at such times as are specified in the Letter of Credit. Each drawing honored by the Bank under the Letter of Credit will immediately reduce the Stated Amount by the amount of such drawing, subject to reinstatement on the terms set forth in the Letter of Credit. All drawings under the Letter of Credit will be paid with the Bank's own funds.

## **Reimbursement Agreement**

(to be conformed when draft Reimbursement Agreement is received)

The Bonds are initially supported by the Initial Letter of Credit which will be issued by the Bank pursuant to the provisions of the Reimbursement Agreement. The Bank has entered into the Reimbursement Agreement with the District providing for, among other things, the District's reimbursement to the Bank of all amounts drawn upon under the Letter of Credit.

The Reimbursement Agreement provides for commitment fees, drawing fees, transfer fees and other fees and charges. The District's obligations under the Reimbursement Agreement are to be secured by the Net Revenues and Taxes.

The District has made comprehensive representations and warranties about itself and its operations in the Reimbursement Agreement to induce the Bank to issue the Initial Letter of Credit. These representations and warranties include, among others, \_\_\_\_\_. The Reimbursement Agreement contains affirmative and negative covenants and reporting requirements. The covenants of the District include, among others: \_\_\_\_\_. Reporting requirements include requirements to furnish \_\_\_\_\_.

The Reimbursement Agreement also sets out certain Events of Default. These include, among others: (i) failure to pay any amount due the Bank; (ii) any attachment of Trust Agreement or Installment Agreement funds; (iii) failure of any representation or warranty to have been true in any material respect; (iv) loss of tax exemption; (v) any default under documents entered into with the Bank or if any event of default occurs under the Trust Agreement or Installment Agreement; (vi) dissolution or insolvency of the District or bankruptcy, reorganization or similar proceedings affecting the District, other than involuntary proceedings dismissed within 60 days; (vii) any execution or similar process in excess of \$500,000 remaining outstanding against the District for 10 days; (viii) failure to maintain required permits or licenses; (ix) failure to comply with governmental regulatory agreements affecting the Project; (x) failure

to maintain insurance on the Project, to protect against liens, or failure to perform covenants in the Reimbursement Agreement within certain cure periods; (xi) default under any other indebtedness of the District; and (xii) failure to comply with its financial covenants.

Upon the occurrence of an Event of Default under the Reimbursement Agreement, the Bank may: (i) call all or a portion of the 1996 Certificates for redemption in accordance with the Trust Agreement; (ii) declare a mandatory tender of the 1996 Certificates in accordance with the Trust Agreement; (iii) request that all 1996 Certificates be tendered for purchase as 1996 Certificates to be owned by the Bank; (iv) enforce its rights against the District through legal action; and (v) exercise other remedies under applicable law or other agreements.

The Bank and the District may, from time to time, amend the Reimbursement Agreement without notice to, or consent of, the Trustee or the Owners.

## **THE BANK**

*The following information has been provided by the Bank for use in this Reoffering Memorandum. Such information has not been confirmed or verified by the District or the Remarketing Agent. Neither the District nor the Remarketing Agent make any representation as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof. Further, no representation is made herein that the information contained or incorporated herein by reference is correct as of any time subsequent to the date hereof.*

### **Union Bank, N.A.**

Union Bank is a full-service commercial bank providing an array of financial services to individuals, small businesses, middle-market companies, and major corporations. The Bank operates 401 branches and 617 ATM's in California, Oregon, Washington, and Texas, as well as two international offices. The Bank serves corporate clients across the country, and has a retail customer base of approximately 1 million households.

Union Bank, N.A. is the primary subsidiary of UnionBanCal Corporation, the second-largest commercial bank holding company headquartered in California, based on assets of \$80.6 billion at March 31, 2011. UnionBanCal is a wholly owned subsidiary of The Bank of Tokyo-Mitsubishi UFJ, Ltd., and a member of the Mitsubishi UFJ Financial Group (MUFG, NYSE:MTU), one of the world's largest financial organizations.

For the quarter ending March 31, 2011, the Corporation had loans totaling \$48.1 billion, total assets of \$80.6 billion and total deposits of \$58.7 billion. For fiscal year ended December 31, 2010, a net income of \$573.0 million was reported, compared with a net loss of \$65 million for full year 2009. Copies of the latest annual report and the most recent quarterly report may be obtained at [www.unionbank.com](http://www.unionbank.com) or at the Bank's Los Angeles office, located at 445 South Figueroa Street, Los Angeles, California 90071.

# SOURCES OF PAYMENT FOR THE CERTIFICATES

## General

Each 1996 Certificate represents a direct, undivided fractional interest in the Installment Payments to be made by the District to the Corporation under the Installment Sale Agreement. The Corporation has assigned all of its rights under the Installment Sale Agreement, including its rights to receive Installment Payments from the District and its remedies under the Installment Sale Agreement to the Trustee for the benefit of the Owners of the 1996 Certificates. The Installment Payments are sufficient to pay, when due, the annual principal and interest represented by the 1996 Certificates.

## Installment Payments

Pursuant to the Installment Sale Agreement, the District is obligated to make Installment Payments solely from Taxes and Net Revenues. The combined totals of such Installment Payments equals the principal and interest due with respect to the 1996 Certificates. The obligation of the District to make the Installment Payments is absolute and unconditional, and until such time as the Purchase Price shall have been paid in full (or provision for the payment thereof shall have been made pursuant to the Installment Purchase Agreement), the District will not discontinue or suspend any Installment Payment required to be made by it under the Installment Sale Agreement when due, whether or not the Water System or any part thereof is operating or operable or its use is suspended, interfered with, reduced or curtailed or terminated in whole or in part, and such payments shall not be subject to reduction whether by offset or otherwise and shall not be conditional upon the performance or nonperformance by any party of any agreement for any cause whatsoever.

**The District's obligation to make the Installment Payments is a limited obligation of the District payable solely from Taxes and Net Revenues of the Water System, and neither the full faith and credit nor the taxing power of the District, the State of California or any of its political subdivisions is pledged for the payment of the 1996 Certificates.**

## Taxes and Net Revenues

The Installment Payments securing the 1996 Certificates are payable from Taxes and Net Revenues on a parity with installment payments securing the District's 2004 Certificates and the 2007 Certificates and the Otay Water District Financing Authority's 2010 Bonds.

"Taxes" means all taxes, including *ad valorem* taxes of the District, other than taxes imposed pursuant to Chapter 1 of Part 9 of the Law to secure general obligation bonds of the District or any improvement district thereof.

"Revenues" means (i) all water availability charges imposed pursuant to Chapter 2 of Part 5 of the Law not exceeding \$10 per acre per year; (ii) all income, rents, rates, fees, charges and other moneys derived by the District from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (a) all income, rents, rates, fees, charges or other moneys derived from the sale, furnishing, and supplying of water and other services, facilities and commodities sold, furnished or supplied through the facilities of the Water System, including connection fees, (b) the earnings on and income derived from the investment of such income, rents, rates, fees and charges or other moneys, (c) the proceeds derived by the District directly or indirectly from the sale, lease or other disposition of a part of the Water System as permitted under the Installment Purchase Agreement and (d) Interest Subsidy Payments; provided that the term "Revenues" shall not include customers' deposits or any other deposits subject to refund until such deposits have become the property of the District.

“Operation and Maintenance Costs” means (i) costs spent or incurred for maintenance and operation of the Water System calculated in accordance with generally accepted accounting principles, including (among other things) the reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the District that are charged directly or apportioned to the Water System, including but not limited to salaries and wages of employees, payments to the Public Employees Retirement System, overhead, insurance, taxes (if any), fees of auditors, accountants, attorneys or engineers and insurance premiums, and including all other reasonable and necessary costs of the District or charges (other than debt service payments) required to be paid by it to comply with the terms of the Bonds or of the Installment Purchase Agreement or any Contract or of any resolution or indenture authorizing the issuance of any Bonds or of such Bonds; and (ii) costs spent or incurred in the purchase of water for the Water System; but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature and all capital charges.

“Net Revenues” means, for any Fiscal Year or other 12-month period, the Revenues for such Fiscal Year or other 12-month period less the Operation and Maintenance Costs for such Fiscal Year or other 12-month period. See “Rate Covenant” and “Parity Debt” herein.

“Interest Subsidy Payment” means cash subsidy payments entitled to be received by the District from the United States Treasury with respect to the 2010B Bonds and any Parity Bonds issued and Contracts executed by the District, including but not limited to “Build America Bonds” issued as contemplated by the American Recovery and Reinvestment Act of 2009.

The District will timely submit all required documentation to the United States Treasury and take any and all action necessary to receive and collect the Interest Subsidy Payments.

## **Allocation of Taxes and Revenues**

Pursuant to the Installment Sale Agreement, the 2004 Installment Purchase Agreement, the 2007 Installment Purchase Agreement and the 2010 Installment Purchase Agreement (collectively, the “Agreements”), the District established separate special funds, the “Revenue Fund” and the “Tax Fund.” Under the Agreements, the District has agreed to deposit all Revenues in the Revenue Fund and all Taxes in the Tax Fund. The Revenues and Taxes will not be used for any other purpose while any of the installment payments due under the Agreements remain unpaid, except as described below. Under the terms of the Agreements, the District will, from moneys in the Revenue Fund, pay Operation and Maintenance Costs (including amounts reasonably required to be set aside in contingency reserves for Operation and Maintenance Costs, the payment of which is not then immediately required) as they become due and payable.

All moneys in the Tax Fund, and, to the extent such moneys are insufficient, all remaining moneys in the Revenue Fund, shall be set aside by the District at the following times in the following respective special funds in the following order of priority and all moneys in each of such funds shall be held in trust and shall be applied, used and withdrawn only for the purposes described herein:

- (a) *Certificate Payment Fund.* On or before each Installment Payment Date, the District shall, from the moneys in the Tax Fund and, to the extent needed, the Revenue Fund, transfer to the Trustee for deposit in the Certificate Payment Fund, the Installment Payment due and payable on that Installment Payment Date. The District shall also, from the moneys in the Tax Fund and, to the extent needed, the Revenue Fund, transfer to the applicable trustee or payee for deposit in the applicable payment fund, without preference or priority, and in the event of any insufficiency of such moneys ratably without any discrimination or preference, payments due under the Agreements and payments with respect to any additional Contracts.

No deposit need be made in the Certificates Payment Fund as Installment Payments if the amount in the Certificates Payment Fund is at least equal to the amount of the Installment Payment due and payable on the next succeeding Installment Payment Date.

All money in the Certificates Payment Fund shall be used and withdrawn by the Trustee in accordance with the Trust Agreement.

- (b) *Reserve Fund.* On or before each Installment Payment Date, the District shall, from the remaining moneys in the Tax Fund and, to the extent needed, the Revenue Fund, thereafter, without preference or priority, and in the event of any insufficiency of such moneys ratably without any discrimination or preference, transfer to the applicable trustee for deposit to such other reserve fund or account for the Existing Parity Obligations and payments with respect to any additional Contracts an amount equal to the amount required to be deposited therein, and to transfer to any insurer any amounts due pursuant to any agreement related to the repayment of draws under a Reserve Policy.

No transfer of moneys for deposit to the Reserve Fund in connection with the Installment Payments need be made if the amount contained therein is at least equal to the Reserve Fund Requirement.

- (c) *Surplus.* Moneys on deposit in the Tax Fund or Revenue Fund not necessary to make any of the payments required above or as required under the Agreements or with respect to any additional Contracts may be expended by the District at any time for any purpose permitted by law.

## **Event of Default and Acceleration of Maturities**

The Installment Payments are payable only from Taxes and Net Revenues and are not secured by, and the 1996 Certificate Owners have no security interest in or mortgage on the property of the Water System or any other assets of the District. Should the District default, the Trustee, as assignee of the Corporation, shall have the right at its option and without any further demand or notice, but subject in all respects to the provisions of the Trust Agreement, declare the entire principal amount of the unpaid Installment Payments and the accrued interest thereon to be due and payable immediately, and upon any such declaration the same shall become immediately due and payable, anything contained in the Installment Sale Agreement to the contrary notwithstanding. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE TRUST AGREEMENT - Default and Limitation of Liability" and "SUMMARY OF CERTAIN PROVISIONS OF THE INSTALLMENT PURCHASE AGREEMENT - Events of Default and Remedies."

## **Rate Covenant**

Pursuant to the Agreements, the District will fix, prescribe, revise and collect rates, fees and charges for the Water Service which will be at least sufficient to yield during each Fiscal Year Taxes and Net Revenues equal to 125% of the Debt Service (including for purposes of such calculation the obligation of the District to repay costs related to any surety bond, reserve credit facility or other reserve fund funding instrument) on the 1996 Certificates, the Existing Parity Obligations and additional Contracts or Parity Bonds (as defined herein) for such Fiscal Year. The District may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Taxes and Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of the Agreements.

For purposes of calculating the ratio required by the rate covenant, when the Existing Parity Obligations are no longer outstanding, the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

For the purposes of the calculations described above, the adjustments to Net Revenues and Debt Service relating to the Interest Subsidy Payments will be made when the Existing Parity Obligations are no longer outstanding with respect to the 2010B Bonds or with respect to any Parity Bonds or additional Contracts that are designated as "Build America Bonds." See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

## **Parity Debt**

Pursuant to the Agreements, the District may at any time execute any contract or issue any bonds the payments under or of which are on a parity with the Installment Payments ("Contracts" or "Parity Bonds"), as the case may be, provided an Independent Financial Consultant or Certified Public Accountant shall render to and file with the District and the Trustee a written report certifying that Taxes and Net Revenues for any twelve (12) consecutive calendar months in the eighteen (18) calendar months immediately preceding the issuance of the additional Contracts or Parity Bonds adjusted as set forth below are at least equal to 125% of Debt Service (including for purposes of such calculation the obligation of the District to repay costs related to any surety bond, reserve credit facility or other reserve fund funding instrument), assuming such additional Contracts had been executed or Parity Bonds had been issued at the beginning of such twelve-month period.

For purposes of calculating the ratio required for the issuance of additional Contracts or Parity Bonds, when the Existing Parity Obligations are no longer outstanding (with the exception of the 2010 Bonds), the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

For the purposes of the calculations described above, the adjustments to Net Revenues and Debt Service relating to the Interest Subsidy Payments will be made when the Existing Parity Obligations are no longer outstanding with respect to the 2010B Bonds or with respect to any Parity Bonds or additional Contracts that are designated as "Build America Bonds."

For purposes of calculating Net Revenues as set forth in the preceding paragraph, adjustments to the computations of Net Revenues may be made for the following:

- (1) any change in service charges which has been adopted subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts;
- (2) customers added to the Water System subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts;
- (3) the estimated change in Net Revenues which will result from the connection of existing residences or businesses to the Water System within one year following completion of any project to be funded or system to be acquired from the proceeds of such Parity Bonds or additional Contracts; and

- (4) the estimated change in Net Revenues which will result from services provided under any long-term, guaranteed contract that extends for the life of the Parity Bonds or additional Contracts if entered into subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts.

Notwithstanding the foregoing, Parity Bonds issued or additional Contracts executed to refund Parity Bonds or additional Contracts (including refunding of the Existing Parity Obligations or the Bonds), may be delivered without satisfying the conditions set forth above if Debt Service in each Fiscal Year after the Fiscal Year in which such Parity Bonds are issued or additional Contracts executed is not greater than Debt Service would have been in each such Fiscal Year prior to the issuance of such Parity Bonds or execution of such additional Contracts. Further, for the purpose of calculating Debt Service for any Parity Bonds or additional Contracts which bear a variable interest rate, the rate of interest used to calculate Debt Service shall be 110% of the greater of (i) the then current variable interest rate borne by such Parity Bonds or additional Contracts (which includes outstanding 1996 Certificates) plus 2%, and (ii) the highest variable rate borne over the preceding 12 months by outstanding variable rate debt issued by the District or, if no such variable rate debt is at the time outstanding, by variable rate debt of which the interest rate is computed by reference to an index comparable to that to be utilized in determining the interest rate for the debt then proposed to be issued. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

In addition to the foregoing, in the event any amounts that are past due and owing to any insurer of Bonds or with respect to any Contracts, such insurer must provide written consent to the issuance of any additional Bonds or the execution of any Contracts.

## **Property Insurance**

The Installment Sale Agreement requires the District to maintain or cause to be maintained with respect to the properties of the Water System, insurance in such amounts and against such risks (including accident to or destruction of the Water System which are of an insurable nature) as are usually covered in connection with facilities similar to the Water System so long as such insurance is available at reasonable costs (see "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE INSTALLMENT SALE AGREEMENT - Insurance" herein). Any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and in the manner usually maintained in connection with water systems similar to the Water System. All proceeds of insurance against property damage and all proceeds of condemnation awards relating to the Project shall be payable to the District alone, and the District shall retain and collect such proceeds. All claims under any such insurance policy or with respect to any condemnation proceeding relating to the Project may be settled by the District without the consent of the Corporation or the Trustee. Such proceeds shall be applied promptly to the optional prepayment of Installment Payments, or retained by the District and promptly applied to the repair or rebuilding of the Project or the acquisition or construction of the capital improvements to the Water System. See "THE CERTIFICATES - Prepayment - Prepayment From Net Proceeds of Insurance and Condemnation" herein. See also "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE INSTALLMENT SALE AGREEMENT - Insurance" herein.

## OTAY WATER DISTRICT

The District was formed in January 1956 pursuant to Section 71000 et seq., of the California Water Code, and joined the San Diego County Water Authority (which is a member of the Metropolitan Water District of Southern California) in September 1956 to acquire the right to purchase and distribute imported water throughout its service area. The District's boundaries currently encompass an area of approximately 125 square miles in San Diego County, lying immediately east of the San Diego metropolitan area and running from the City of El Cajon south to the Mexican border, abutting the cities of El Cajon and La Mesa, and encompassing most of the City of Chula Vista and a small portion of the City of San Diego (the "Service Area"). The District is the sole provider of water in the Service Area. Approximately 39% of the geographic Service Area is currently developed, and this percentage will continue to increase as the District's Service Area continues to develop and grow. The District's water sales by volume increased by 7.5% per year from 2004 to 2007. Since 2007, new residential construction has declined significantly and there has been little growth in residential connections. However, the District continues to add connections to both its potable and recycled water system at a slow rate. As of June 30, 2010, the District had nearly 48,000 potable and 700 recycled service accounts representing a population of approximately 206,000, with an average daily demand of 30.5 million gallons per day (mgd). Ultimately, the District is projected to serve 277,000 people, creating an average daily demand of 56.3 mgd.

Most potable water delivered by the District is purchased from the San Diego County Water Authority ("SDCWA") who in turn purchases water from the region's water importer, the Metropolitan Water District of Southern California and QSA supplies. In Fiscal Year 2007, the District entered into an agreement with the City of San Diego to treat raw water to potable level before being introduced to the District's Water System. A small amount of potable water has also been purchased from the City of San Diego, and will be purchased in the future on an as needed basis. By taking raw water through SDCWA's system at a different connection, there is increased reliability of water supplied to the District. In addition, the Jamacha Road Pipeline Project provides increased capacity with the connection to SDCWA, where the District has established an additional delivery point for treated water from the Helix Water District Levy treatment plant. Water delivered through the new pipeline will be stored in two recently constructed 10 million gallon reservoirs. The District is also moving forward with a ground water project which will provide an additional source of water.

The District owns and operates a recycled water distribution network. Recycled water from the District's Ralph W. Chapman Water Recycling Facility ("RWCWRF") is used to irrigate golf courses, landscaping at schools, public parks, roadway landscapes, and various other approved uses in eastern Chula Vista. The RWCWRF is capable of reclaiming wastewater at a rate of approximately 1.2 million gallons per day. The District is also in a partnership with the City of San Diego to beneficially reuse an additional 6 million gallons per day of recycled water from the City of San Diego's South Bay Reclamation Plant (since Spring of 2007), which required the District to construct over six miles of connecting pipeline, a pump station and a 12 million gallon reservoir. Using this new resource to meet recycled water demands on the Water System has resulted in the District being able to allocate approximately 3,100 acre-feet per year of potable water to other uses.

The District also owns and operates a wastewater collection and reclamation system, providing public sewer service to approximately 4,656 customers within the Jamacha drainage basin. This wastewater system is not a part of the Water System.

The District is administered by a Board of Directors consisting of five members who are elected to four-year alternating terms by the voters residing within the District's boundaries. The District is divided into five divisions, with each Director representing a specific division within which he or she must reside. The current members of the Board and key administrative personnel are:

### **DIRECTORS**

Jaime Bonilla, *President - Division 2*  
Gary D. Croucher, *Vice President - Division 3*  
David Gonzalez, Jr., *Treasurer - Division 1*  
Jose Lopez, *Division 4*  
Mark Robak, *Division 5*

### **MANAGEMENT TEAM**

Mark Watton, *General Manager*  
German Alvarez, *Assistant General Manager Finance & Administration*  
Manny Magaña, *Assistant General Manager Engineering & Operations*  
Joseph R. Beachem, *Chief Financial Officer*  
Rom Sarno, Jr., *Chief of Administrative Services*  
Geoff Stevens, *Chief Information Officer*  
Rod Posada, *Chief of Engineering*  
Pedro Porras, *Chief of Water Operations*

Under direction of the General Manager, the District has 159 employees.

## **THE WATER SYSTEM**

The following information concerning the Water System was obtained from District officials except where otherwise indicated. The audited financial statements of the District for the Fiscal Year ended June 30, 2010 are attached hereto as "APPENDIX B" and should be read in their entirety.

### **Existing Facilities**

Potable Water Facilities - The principal facilities of the existing potable water system consist of six water supply connections with SDCWA, one water supply connection with the City of San Diego, 24 pump stations, over 709 miles of pipelines, and 40 storage reservoirs.

The District currently receives treated potable water from the SDCWA through four connections to one of the pipelines owned and operated by the SDCWA. This water is treated by the Metropolitan Water District of Southern California at its Skinner Water Treatment Plant and SDCWA at its Twin Oaks Treatment Plant. In addition, the District currently receives treated potable water from the SDCWA through one connection to the Helix Water District water system. This water is be treated by the Helix Water District at its R.M. Levy Water Treatment Plant pursuant to an agreement with the SDCWA. The District may also purchase treated potable water, if available, from the City of San Diego. This water is sold by the SDCWA to the District in raw form and delivered to the City of San Diego's Otay Water Treatment Plant pursuant to an agreement among the SDCWA, the District and the City of San Diego. These supply sources and connecting transmission mains deliver water to terminal storage reservoirs that provide water service to customers within the Service Area.

Recycled Water Facilities - The principal facilities of the existing recycled water system consist of 2 recycled water supply sources, 3 pump stations, 96 miles of pipelines, and 4 storage reservoirs.

The District currently produces recycled water at the RWCWRF, which is owned and operated by the District. Recycled water from the RWCWRF and some of the District’s treated potable water supply are delivered into storage reservoirs that provide recycled water service to recycled water customers.

The District is divided into five geographic areas. These five areas contain five potable water systems and two recycled water systems. The systems are called Hillsdale, Regulatory, La Presa, Central Area, and Otay Mesa. The Hillsdale, Regulatory, and La Presa systems are collectively referred to as the North District, while the Central Area and Otay Mesa systems are collectively referred to as the South District. Recycled water service is currently limited to the South District. There are multiple pressure zones within each system, except Otay Mesa.

**North District.** The Hillsdale system includes the extreme north part of the District’s Service Area. The Regulatory system is located between the Hillsdale and La Presa systems. The Regulatory system reservoirs are considered to provide emergency storage for the entire North District as well as some operational storage for the 640 and 520 Pressure Zones. Two new 10 million gallon reservoirs are located within the Regulatory system and provide storage for the treated water delivered through the new 36 inch pipeline, which connects to the Helix Water District system by way of the SDCWA aqueduct. The La Presa system is generally located north and east of the Sweetwater reservoir and is the southernmost system of the North District.

**South District.** The Central Area system is roughly bounded by Interstate 805 on the west, Otay River on the south, the Lower Otay Reservoir on the east, and the Regulatory System on the north. Three Central Area system reservoirs provide emergency storage for the entire Central Area system and also provide operational storage for the 624 Pressure Zone. Additional reservoirs provide operational storage for other pressure zones throughout the Central Area. The Otay Mesa system includes the extreme south portion of the District Service Area and is generally located between the Otay River on the north and the Mexico border on the south. The South District has experienced, and is expected to experience, the most growth in the District’s Service Area.

## Water Storage

The District currently operates 41 potable and 4 recycled reservoirs as shown below with a total capacity of 263 mg. The District estimates that the reservoirs are between 75% and 80% full on a typical day.

<u>System</u>	<u>Reservoirs</u>	<u>Capacity (mg)</u>
Hillsdale	6	13.9
Regulatory	13	48.7
La Presa	9	23.7
Central Area	11	85.5
Otay Mesa	2	47.7
Recycled	<u>4</u>	<u>43.7</u>
Total	45	263.2

## Water Supply

**Service Area Water Supply - Potable.** The District does not have a local source of surface water, and is working to complete a modest supply of ground water. The District purchases a significant amount of its potable water from the SDCWA. Under a contractual arrangement with the SDCWA, the District also receives potable water from the Helix Water District's Levy Water Treatment Plant and from the City of San Diego.

The SDCWA implemented a water rate increase on January 1, 2010, which resulted in an approximate 11.3% increase for the District's cost of purchased potable water from SDCWA. SDCWA has provided preliminary estimates on water cost increase expected to be implemented by SDCWA January 1, 2011. The overall cost increase is expected to be 7.5%.

**Service Area Water Supply - Recycled.** The District produces approximately 1.2 mgd of recycled water at the RWCWRF. The District has contracted with the City of San Diego to purchase up to 6 mgd of recycled water produced by the City of San Diego's South Bay Water Reclamation Plant. Construction on the required pump station, reservoir, and the 6-mile delivery system allowing the District to connect to the City of San Diego's recycled water pipeline was completed in 2007.

**SDCWA Water Supply.** For Fiscal Year 2010, approximately 87% of the region's water supply came from imported water, with the remainder coming from member agency's local supplies. Of the purchased supply, 71% is from the Metropolitan Water District of Southern California ("MWD"). For the Fiscal Year ended June 30, 2010, the SDCWA supplied the District 31,168 acre-feet of water (quantities of water are expressed in terms of acre-feet which is the amount of water which will cover one acre to a depth of one foot and is equivalent to approximately 326,000 gallons and approximately the average annual water usage of two households).

As an alternative to purchasing all of its imported water from MWD, the SDCWA has begun to diversify its purchases through core and spot water transfers with other agencies. Since 2003, the SDCWA has been receiving a portion of its imported water pursuant to the terms of the Quantification Settlement Agreement ("QSA") among the State of California acting by and through the Department of Fish and Game, the Coachella Valley Water District ("CVWD"), the Imperial Irrigation District ("IID") and the SDCWA, executed on October 10, 2003, the Water Transfer Agreement (defined below) and other QSA related agreements. Water that the SDCWA receives from IID is conveyed through the Colorado River Aqueduct pursuant to an exchange agreement with MWD. The SDCWA began receiving transfer water from IID in December 2003. Starting with the initial delivery of 10,000 acre-feet, the amount of water to be delivered is increasing according to an agreed-upon schedule until the maximum transfer yield of 200,000 acre-feet per year is achieved. In addition, the SDCWA will receive approximately 77,000 acre-feet of imported water per year from water conserved through the lining of the All-American Canal Lining Project and the Coachella Canal Lining Project. The SDCWA began receiving water from the Coachella Canal Lining Project in 2007 and in 2010 will receive its full allotment from the All-American Canal Lining Project. The SDCWA is also pursuing spot water transfers to provide supplemental supplies to the region during times of supply shortages. Spot transfers are short-term transfers or leases, typically agreed to and completed within one to three years.

Litigation related to the QSA is described in "APPENDIX F - INFORMATION CONCERNING METROPOLITAN WATER DISTRICT'S WATER SUPPLY - QSA-Related Litigation."

The SDCWA continues to pursue supply diversification efforts for itself and the region, including long-term planning, recycling of local surface water, groundwater, recycled water, local seawater desalination and conservation efforts.

Water Storage facilities are also critical to assuring consistent water availability notwithstanding fluctuation in available supply. The SDCWA has recently entered into agreements to expand available storage capacity. The SDCWA recently issued over \$600 million in water bonds to finance its Capital Improvement Program. One of the purposes of the Capital Improvement Program is to interconnect a number of member agency storage facilities. Another purpose is to enhance the SDCWA's own storage capacity.

The SDCWA faces various challenges in the continued supply of water to the District and other member agencies. A description of these challenges as well as a variety of other operating information with respect to the SDCWA is included in certain disclosure documents prepared by SDCWA. The SDCWA has entered into certain continuing disclosure agreements pursuant to which SDCWA is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 of the Exchange Act ("Rule 15c2-12") and annual audited financial statements (the "SDCWA Information") with the Municipal Securities Rulemaking Board which are available online at [www.emma.msrb.org](http://www.emma.msrb.org).

**SDCWA HAS NOT REVIEWED THIS REOFFERING MEMORANDUM AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO SDCWA. SDCWA IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH SDCWA INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

**MWD Water Supply.** The SDCWA currently purchases all of its imported water from MWD and IID. SDCWA is MWD's largest member agency, purchasing approximately [24%] of MWD's supplies in Fiscal Year 2009/10. MWD obtains its water supply from two primary sources: the Colorado River, via MWD's Colorado River Aqueduct, and the State of California Department of Water Resources' State Water Project ("SWP"), via the Edmund G. Brown California Aqueduct.

MWD faces various challenges in the continued supply of imported water to SDCWA and other member agencies. A description of these challenges as well as a variety of other operating information with respect to MWD is included in "APPENDIX F" hereto and in certain disclosure documents prepared by MWD. MWD has entered into certain continuing disclosure agreements pursuant to which MWD is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 and annual audited financial statements (the "MWD Information") with the Municipal Securities Rulemaking Board which are available online at [www.msrb.org](http://www.msrb.org).

**MWD HAS NOT REVIEWED THIS REOFFERING MEMORANDUM AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO MWD. MWD IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH MWD INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

**Historic and Projected Water Supply.** As noted, the State of California has experienced drought conditions for several years, which have impacted the SDCWA's base allocation of water to the District. The District's base allocation of potable water is 43,162 acre feet. In 2009, SDCWA implemented an 8% reduction in the base allocation to its customers, resulting in an allocation to the District of 39,680.6 acre feet. On April 28, 2011, SDCWA announced the end of mandatory water use restrictions and that there will no longer be a reduced water allocation for member agencies

At its peak in Fiscal Year 2006/07, the District purchased 41,909 acre feet of potable water from SDCWA. Of this amount, 3,073 acre feet of potable water was used to provide water to the customers of the District's recycled water system. However, the District has developed additional sources of recycled water and no longer needs to purchase potable water to supplement the recycled system. This has resulted in a reduction of purchased water from SDCWA from a high of 41,909 acre feet in Fiscal Year 2006/07 to 31,168 acre feet in Fiscal Year 2009/10, well below the current reduced allocation of 39,680.6 acre feet. Purchased water from SDCWA is expected to be maintained at approximately 21% below the reduced allocation and 26% below the District's projected highest demand year for the next several years.

Set forth below is a summary of the District's sources of water supply for the last eight Fiscal Years.

#### HISTORIC WATER SUPPLY IN ACRE-FEET PER YEAR

<u>Fiscal Year Ended June 30</u>	<u>Produced Recycled Water</u>	<u>Purchased Recycled Water</u>	<u>Purchased Potable Water</u>	<u>Total</u>
2003	1,117	0	34,539	35,656
2004	1,305	0	38,918	40,223
2005 <sup>(1)</sup>	1,150	0	37,678	38,828
2006	1,234	0	40,946	42,180
2007 <sup>(2)</sup>	1,263	653	41,909	43,825
2008	1,235	3,595	38,045	42,875
2009	844 <sup>(3)</sup>	3,686	34,971	39,501
2010	1,032	2,871	31,168	35,071

Source: Otay Water District.

<sup>(1)</sup> Rainfall in 2005 was significantly above average, resulting in decreased purchases of potable water and production of recycled water.

<sup>(2)</sup> After the District began purchasing recycled water from the City of San Diego in May of 2007, it was no longer necessary to purchase potable water for the recycled system to supplement the amount of produced recycled water. See "Water Supply - Service Area Water Supply - Recycled" above.

<sup>(3)</sup> The treatment plant was not in operation for a total of 74 days in Fiscal Year 2008/09 for planned maintenance.

The District currently expects that demand for potable water may reach as high as 60,000 acre feet per year at buildout, potentially by the year 2040. In order to provide enough water to meet expected demand at buildout, the District continues to develop additional sources of water.

Currently, the District is negotiating a long term purchase contract for potable desalinated water. The desalinization plant, if constructed, would be located in Mexico. The plant is likely to take several years to complete, and is estimated to produce 100,000 acre feet of desalinated water annually. If constructed, it is expected that an approximate 24,000 acre feet of water could initially be supplied to the District from this source. This water supply would be delivered to the District's boundary coincident with the United States and Mexican international border. In order to take delivery of such water supply, the District needs to construct a conveyance system, within the District, from that delivery point to the District's distribution system. The construction includes 3.2 miles of pipeline, a pump station and a water treatment plant. The District expects that the conveyance system would take approximately 3 years to construct and the District would commence construction if a purchase contract is entered into.

As noted, the District is currently negotiating terms of the purchase contract, which may include a take-or-pay arrangement for all contracted water amounts. Water purchases under such a contract would be payable as an Operation and Maintenance Cost of the District, similar to the current water purchases from SDCWA and other existing sources. The District projects no appreciable difference in the cost of such water compared to current estimated costs of water purchased from SDCWA.

If the desalination plant is completed, the District would expect to reduce the amount of water it purchases from SDCWA. However, should water from the desalination plant be unavailable, as a member of SDCWA, the District would be entitled to request additional water purchases from SDCWA. The District believes that such a transition back to increased SDCWA water purchases could require temporary rate increases but would not have a material adverse effect on the District's financial condition.

The District makes no guarantee that the desalination plant will be constructed, and if so constructed, cannot guarantee construction in accordance with the timelines described herein. The District also provides no assurance that any contractual arrangement for the purchase of water from the facility will be executed with the terms described herein.

The District also continues to convert existing potable connections to the recycled water system when possible. In addition, the District anticipates converting a significant number of potable connections in the Gray Mesa area to the recycled system once the required pipelines are put in place, estimated to occur in four to five years.

Set forth below is a summary of the District's projection of water sources for the current and five succeeding Fiscal Years and includes desalinated water purchases in the "Purchased Potable Water" column beginning in 2013.

**PROJECTED WATER SUPPLY IN ACRE-FEET PER YEAR**

<b>Fiscal Year Ending June 30</b>	<b>Produced Recycled Water <sup>(1)</sup></b>	<b>Purchased Recycled Water</b>	<b>Purchased Potable Water <sup>(2)</sup></b>	<b>Total</b>
2011	1,202	2,946	30,142	34,290
2012	854 <sup>(3)</sup>	3,105	30,438	34,397
2013	1,100	3,041	30,971	35,112
2014	1,100	3,126	31,522	35,748
2015	1,100	3,156	31,897	36,153
2016	1,100	3,196	32,296	36,592

Source: Gray Water District

<sup>(1)</sup> Maximum capacity for the treatment plant is 1,450 acre feet, but the District bases its projection of 1,100 acre feet on normal (efficient) capacity.

<sup>(2)</sup> Includes purchases from SDCWA, raw water treated to potable level by the City of San Diego and the Helix Water District, and assumes desalinated water purchases.

<sup>(3)</sup> In Fiscal Year 2012, the District plans work on the treatment plant, lowering production temporarily and increasing recycled purchases.

## Capital Improvement Program

The District boundaries encompass areas of San Diego County that experienced rapid growth between 2001 and 2007, and significant growth is expected in future years. The District currently serves a population of approximately 206,000. Ultimately, the District is projected to serve 277,000 people and it estimates an additional \$350 million investment in capital assets will be required through ultimate buildout, over 20 years.

The District has developed a six-year Capital Improvement Program (the "CIP") based on future water demands in its Service Area. The District reviews and updates the CIP at least annually based on an analysis of the potable and recycled water demands most recently projected by developers, demographics, and population estimates by the San Diego Association of Governments. Major capital improvements within the next six years are planned in order to provide facilities to deliver water to new customers and to acquire additional water and recycled water capacity. These facilities are categorized by the District into those improvements relating to the Water System, which includes recycled water. Within each segregated operational area, the CIP is further separated into improvement categories – Expansion, Betterment and Replacement.

The table below summarizes the current six-year \$155 million Capital Improvement Program for the Water System and the categories of work to be completed.

	Fiscal Year Ending June 30						Total
	2012	2013	2014	2015	2016	2017	
Expansion	\$ 4,866,000	\$ 3,972,000	\$ 3,965,000	\$ 4,033,000	\$ 7,890,000	\$20,789,000	\$ 44,515,000
Betterment	6,472,000	4,385,000	9,279,000	5,970,000	9,420,000	11,700,000	47,426,000
Replacement	9,774,000	11,869,000	8,266,000	8,155,000	8,619,000	2,135,000	48,818,000
New Supply	<u>1,520,000</u>	<u>1,920,000</u>	<u>6,120,000</u>	<u>3,980,000</u>	<u>120,000</u>	<u>120,000</u>	<u>13,780,000</u>
Total	\$22,632,000	\$21,346,000	\$27,630,000	\$22,138,000	\$26,049,000	\$34,764,000	\$154,559,000

Source: Only Water District.

The District has identified the timing and method of funding the capital improvements over the next six years. Each category of improvements is designed to be funded with operational net cashflow, bond proceeds, transfers between operational areas, other capital related charges, reserves or a combination of these sources. The District expects to fund these improvements with reserves, operating income, investment income, bond proceeds, capacity fees and other fees, grants and additional financing. The District expects that additional financing may occur in 2014. In order to implement the Capital Improvement Program, the District anticipates that it will need to increase its rates as described herein (see "Water Charges" herein). However, there is no guarantee that the District will implement such rate increases at the amount and at the time anticipated in its planning documents. See "Water Charges - Proposition 218."

## Water Service

**Historical Water Use.** Table No. 1 shows the amount of water usage, connections and revenue generated from water and recycled water sales in the last five fiscal years, with estimated amounts for 2010/11. There have been over 1,639 new residential connections between Fiscal Years 2004/05 and 2010/11, an increase of 3%. Population has increased over 37% during this period from 148,000 to over 206,000, accounting for the significant increase in the amount of water usage.

Rainfall in Fiscal Year 2010/11 was above average and above recent years' totals. Together with conservation efforts by customers, this has caused a reduction in water sales in 2010/11 from amounts budgeted by the District. Historical rainfall totals are shown below.

### HISTORICAL RAINFALL

Year	Inches
2006	5.42
2007	3.85
2008	7.49
2009	9.17
2010	11.01
2011 (estimate)	12.27

**TABLE NO. 1**  
**CONNECTIONS AND WATER SALES VOLUME AND REVENUE**  
**Fiscal Years 2005/06 through 2010/11**

	<u>2005/06</u>	<u>2006/07</u>	<u>2007/08</u>	<u>2008/09</u>	<u>2009/10</u>	<u>Estimate</u> <u>2010/11 <sup>(3)</sup></u>
<b>Potable</b>						
Residential - Volume in ccf <sup>(1)</sup>	9,328,713	9,713,112	9,402,189	8,891,191	7,690,858	7,304,151
- Volume in acre feet	21,185	22,298	21,583	20,387	17,659	17,237
Residential - Connections	42,763	43,292	43,342	43,431	43,619	43,849
Residential - Sales Revenue <sup>(2)</sup>	\$ 16,784	\$ 18,695	\$ 17,775	\$ 17,353	\$ 18,389	\$ 19,587
All Others - Volume in ccf	5,875,415	6,346,352	6,173,480	6,042,570	5,058,943	4,811,821
- Volume in acre feet	13,487	14,568	14,171	13,871	11,611	11,046
All Others - Connections	4,088	4,168	4,249	4,257	4,227	4,253
All Others - Sales Revenue <sup>(2)</sup>	\$ (1,191)	\$ 12,002	\$ 13,261	\$ 12,823	\$ 12,979	\$ 12,506
Total Potable Connections	46,851	47,460	47,591	47,688	47,846	48,101
Annual Increase in Connections	809	609	131	97	158	255
<b>Recycled <sup>(4)</sup></b>						
Recycled - Volume in ccf	1,729,000	1,920,287	2,001,137	1,997,882	1,774,565	1,662,529
- Volume in acre feet	3,969	4,408	4,594	4,572	4,073	3,817
Recycled - Connections	558	588	628	671	681	681
Recycled - Sales Revenue <sup>(2)</sup>	\$ 3,086	\$ 3,886	\$ 5,182	\$ 5,499	\$ 6,002	\$ 6,200
Annual Increase in Connections	75	30	38	46	10	0
<b>Total</b>						
Total Volume in ccf	16,830,128	17,979,751	17,376,806	16,913,448	14,524,362	13,978,501
Total Volume in acre feet	38,641	41,274	40,348	38,830	33,336	32,089
Total Connections	47,409	48,048	48,217	48,359	48,527	48,782
Total Sales Revenue <sup>(2)</sup>	\$ 31,041	\$ 34,583	\$ 35,218	\$ 33,873	\$ 37,370	\$ 38,293
Fixed Charges <sup>(5)</sup>	\$ 12,715	\$ 14,023	\$ 15,535	\$ 16,524	\$ 18,840	\$ 19,806
Total Revenue	\$ 43,756	\$ 48,606	\$ 50,753	\$ 52,399	\$ 56,210	\$ 58,199

Source: Oray Water District.

<sup>(1)</sup> ccf refers to a measurement of 100 cubic feet (1 cubic foot = 7.48 gallons).

<sup>(2)</sup> Revenue in \$ Thousands.

<sup>(3)</sup> The District receives a credit from SDCWA and MWD for every acre-foot of recycled water sold. Beginning in May 2007, the District stopped purchasing potable water to supplement the recycled water purchases for the recycled system and since that time the credit has been received on all recycled water sold, and is included in Recycled Sales Revenue.

<sup>(4)</sup> Includes fixed charges, energy charges and delinquency collections on both potable and recycled water sales.

<sup>(5)</sup> The District projects that actual potable sales volume in 2010/11 will be 6% less than budgeted, and actual recycled water sales volume will be 12% less than budgeted. This is a result of above average rainfall, below average temperatures and continued conservation efforts of customers. See "Projected Debt Service Coverage" herein.

Table No. 2 shows the 10 largest water users for Fiscal Year 2009/10.

**TABLE NO. 2  
TEN LARGEST CUSTOMERS BY WATER SALES REVENUES<sup>(1)</sup>**  
Year ended June 30, 2010

Customer	Business Type	Usage in Hundred Cubic Feet	Usage in Acft. Feet	% of Water System Consumption	Water Sales Revenues	% of Total Water Sales Revenues
City of Chula Vista	Public	646,349	1,484	4.5%	\$2,218,584	3.9%
County of San Diego	Public <sup>(2)</sup>	280,563	644	1.6	943,132	1.7
State of California	Public <sup>(3)</sup>	292,077	671	1.6	803,450	1.4
Eastlake III Community Association	Construction/ Irrigation <sup>(4)</sup>	172,267	395	1.0	331,489	0.9
Eastlake Summit Association	Construction	46,898	108	0.3	523,703	0.9
Eastlake Country Club	Irrigation <sup>(4)</sup>	150,809	346	0.8	406,813	0.7
Belleme HOA	Irrigation <sup>(4)</sup>	47,209	108	0.3	397,621	0.7
Chula Vista School District	Public	105,324	243	0.6	377,411	0.7
Cuyamaca College	Public	41,612	96	0.2	354,666	0.6
Sweetwater School District	Public	105,921	243	0.6	348,083	0.6
		1,889,439	4,338	10.5%	\$6,904,952	12.3%

Source: Otay Water District

<sup>(1)</sup> Includes both potable and recycled water sales and excludes fixed charges.

<sup>(2)</sup> George F. Bailey Detention Facility.

<sup>(3)</sup> Richard J. Donovan Correctional Facility.

<sup>(4)</sup> Recycled water use.

## Water Charges

**Water Service Rates.** The District held a public hearing on August 24, 2009 and approved a five-year schedule of rates, which included authorization to raise rates by up to 10% per year during the five year period for costs other than SDCWA, San Diego and MWD rate increases and to pass through all SDCWA, San Diego and MWD increases without limitation during the five year period. A 19.9% rate increase took effect for water usage beginning September 1, 2009 and a 10.9% rate increase took effect for water usage beginning January 1, 2011. The Board of Directors will continue to take action each year to set rates, however they are not expected to need to hold another Proposition 218 hearing for three more years. See "Proposition 218" below.

The District, based on its internal rate model and the need to fund the CIP, increased rates by 7.7% for water usage beginning January 1, 2012. The District anticipates that it will need to increase its rates by approximately 7.7% in each of the next three years and 4.9% in each of the following three years. The largest component of the required rate increases is related to the increase in purchased water costs from SDCWA. For Fiscal Year 2011/12, the expected cost increase provided by SDCWA is greater than the projected 7.7% estimated rate increase by the District.

The water rate structure uses both fixed and variable charges. All customer classes are charged the “monthly fixed charge” based on the meter size as shown in Table No. 3. The commodity or consumption rates as outlined in Table No. 4 are variable in that they are charges per unit. The District also uses an inclining block rate structure for the commodity rate. As a result, each class of customer has a range of rates and for certain classes - commercial, irrigation, and recycled - rates are further differentiated based on meter size. Residential customers (also called domestic customers) have a range of rates beginning at \$2.10 and up to \$4.21 based on the number of units used. The average residential customer uses 15 units of water. One unit of water is equal to 100 cubic feet of water (one cubic foot of water equals 7.48 gallons). Customers outside the District and tanker trucks are charged two times the commodity rate.

**TABLE NO. 3**  
**MONTHLY FIXED CHARGES**  
**As of January 1, 2011**

<u>Meter Size</u>	Domestic Service Monthly <u>Fixed Charge</u>	MWD/SDCWA Additional Monthly <u>Fixed Charge</u>
3/4"	\$ 14.58	\$ 11.82
1"	18.52	19.69
1-1/2"	28.37	39.49
2"	40.18	63.07
3"	71.68	126.14
4"	107.13	197.11
6"	205.59	394.17
8"	323.73	630.71
10"	461.57	903.58
Fire	30.11	

Source: Otay Water District.

**TABLE NO. 4  
COMMODITY RATES  
As of January 1, 2011**

<u>Customer Class: Domestic</u>		<u>Customer Class: Master Meter</u>	
<u>Units<sup>(1)</sup></u>	<u>Charge Per Unit</u>	<u>Units<sup>(2)</sup></u>	<u>Charge Per Unit</u>
Oneline ( Less than 5 hcf)	\$1.49	0-4	\$2.29
6-10	2.31	5-9	2.97
11-22	3.00	Over 9	4.57
Over 23 hcf	4.63		

\* Note: Customers whose total consumption is 10 units or less per month shall receive a benefit of a lower rate for units 1-5. These units will be billed at a rate of \$1.49 per unit.

<u>Customer Class: Commercial</u>		
<u>Less Than 10" Meter:</u>	<u>10" Meter or Greater:</u>	<u>Charge Per Unit</u>
0-173 Units	0-7,426 Units	\$2.44
174-831 Units	7,427-14,616 Units	2.50
Over 832 hcf Units	Over 14,617 Units	2.54

<u>Customer Class: Irrigation</u>			
<u>3/4"-1" inch Meter:</u>	<u>1-1/2"-2" Meter:</u>	<u>3" and Up Meter:</u>	<u>Charge Per Unit</u>
0-49 Units	0-144 Units	0-1,044 Units	\$3.82
50-132 Units	145-355 Units	1,045-8,067 Units	3.39
Over 133 hcf Units	Over 356 hcf Units	Over 8,068 hcf Units	3.45

<u>Customer Class: Recycled</u>				
<u>3/4"-1" Meter:</u>	<u>1-1/2"-2" Meter:</u>	<u>3"-4" Meter:</u>	<u>6" Meter or Greater:</u>	<u>Charge Per Unit</u>
0-42 Units	0-168 Units	0-403 Units	0-7,916	\$2.84
43-97 Units	169-402 Units	404-820 Units	7,917-16,357	2.88
Over 98 Units	Over 403 Units	Over 821 Units	Over 16,358	2.94

Source: Clay Water District

<sup>(1)</sup> 1 unit equals 100 cubic feet of water.

Additionally, commercial-agriculture users participating in MWD or SDCWA conservation programs are eligible to receive discounts from the base agriculture rate. As noted above, the District has estimated that future rate increases will be necessary to implement the current six-year CIP. Additionally, the rates, charges and fees may be increased each year to pass-through increases in costs imposed by SDCWA, San Diego or MWD not already estimated to occur (approximately 89% of the projected rate increases over the next five years relate to estimated increases in SDCWA and MWD charges to the District).

Table No. 5 compares average residential water rates charged by the District with surrounding cities and other water agencies in San Diego County.

**TABLE NO. 5  
COMPARISON OF  
PROPOSED RESIDENTIAL WATER RATES  
As of March 1, 2011**

<u>City/Water Agency</u>	<u>Average Rates <sup>(1)</sup></u>
Lakeside	\$58.28
Oceanside	64.35
Helix WD	64.65
Poway	66.05
Olivenhain Water District	66.95
Yuima Water District	68.17
<b>Otay Water District</b>	<b>69.22</b>
San Dieguito Water District	69.71
San Diego	76.44
Carlsbad	76.74
Vallacitos Water District	77.19
Santa Fe	77.32
Valley Center	78.18
Escondido	79.28
Vista	79.64
Sweetwater Water District	80.86
Ramóna	81.47
Padre Dam Water District - East	82.89
Padre Dam Water District - West	83.16
Rincon	87.91
Fallbrook	91.57
Del Mar	95.05
Rainbow Water District	97.48

Source: Otay Water District

<sup>(1)</sup> Average rates based on assumed residential use of 15 ccf of water monthly.

**Delinquencies.** Accounts receivable that have not been paid in over 60 days represent less than 0.6% of the District's annual sales for the last three fiscal years. Accounts receivable between 30 to 60 days delinquent in payment have averaged 0.9% of the District's annual water sales for the last two fiscal years. In the last three fiscal years, the District has written off less than \$200,000 a year in uncollectible accounts.

The District has implemented a number of changes over the past few years which are significant in improving the management of the accounts receivables. The collection process is more efficient with the introduction of automatic dialers making it possible to address collections of smaller balances. The District has improved the collection process related to properties in foreclosure by collecting deposits and locking all vacant properties. The District has also provided new convenient payment options by introducing payments by phone and web. The District has increased the availability of account information by introducing 24/7 Interactive Voice Response. In addition, with the improvements in online banking systems, the turnaround time on payment processing has decreased from 10 to 2 days. These improvements implemented over the last few years have all assisted the District in better managing

its accounts receivable. The District continues to be focused on finding new ways to assist customers in managing their accounts. Some of the improvements currently being implemented are electronic bill presentation, recurring payments via credit card, and the ability to make water payments at any retailer using the same electronic network used by the District's bank.

**Other Charges.** The District charges an energy charge of \$0.044 per 100 feet of elevation for all connections over a 450 foot elevation. Betterment charges in certain areas ranging from \$.08 to \$.27 per unit to pay for reservoirs, pump stations and other infrastructure. The District also applies additional water development charges in some areas in the North District.

**Capacity Fees and Meter Fees.** The District charges capacity fees to connect to the Water System. Current capacity fees are \$7,697 and the new water supply of \$887 for a single family residential connection, increased quarterly according to the Engineering News-Record index. The District also charges a meter fee for the materials and installation cost of a meter. The meter fees range from \$266 for a single family residence to \$5,507 for a 10" meter.

**Availability Fees.** The District levies and collects annual standby availability charges. Current legislation provides that any availability charge in excess of \$10 per acre shall be used only for the purpose of the improvement district for which it was assessed. Therefore, availability fees shown in Table No. 9 and Table No. 10 include only the first \$10 of availability fees. To the extent the availability fees in excess of \$10 per acre are authorized for operational purposes, they are included in Table No. 9 in "Connection and Other Fees" and in Table No. 10 in "Other Income."

**Annexation Fees.** When service is requested outside the boundaries of the District, the land to be serviced is annexed and an annexation fee is charged by the District. Current annexation fees are \$1,516 for single family residential connections and are adjusted quarterly according to the Engineering News-Record index.

Annexation fees are currently charged for new service that may be within the District boundaries, but outside of an improvement district within the District boundaries. The new annexation fees are expected to apply only to properties outside the District boundaries.

As a result of the change in fee structure, future capacity fees and annexation fees may not be comparable to amounts shown in prior years.

**Proposition 218.** On November 5, 1996, California voters approved Proposition 218, the "Right to Vote on Taxes Act." Proposition 218 added Articles XIII C and XIII D to the State Constitution, which contain a number of provisions affecting the ability of the District to levy and collect both existing and future taxes, assessments, fees and charges. Proposition 218 also extends the initiative power to reducing or repealing any local taxes, assessments, fees and charges. This extension of the initiative power is not limited to taxes, assessments, fees and charges imposed on or after November 6, 1996, the effective date of Proposition 218, and could result in retroactive repeal or reduction in any existing taxes, assessments, fees or charges, except those which are pledged to the repayment of debt. If such provisions were held to apply to the District's fees or charges and a repeal or reduction in District fees or charges were to occur, and it was held that any such taxes, assessments, fees or charges were not pledged to any debt repayment, the District's ability to pay debt service on the Bonds could be adversely affected. It is also possible that the courts would uphold a reduction in rates and charges that reduce the coverage available from Net Revenues below the levels historically maintained by the District.

Article XIII D conditions the imposition or increase of any "fee" or "charge" upon there being no written majority protest after a required public hearing and, for fees and charges other than for sewer, water or refuse collection services, voter approval. Article XIII D defines "fee" or "charge" to mean levies (other than *ad valorem* or special taxes or assessments) imposed by a local government upon a parcel or upon a person as an incident of the ownership or tenancy of real property, including a user fee or charge for a

“property-related service.” One of the requirements of Article XIII D is that before a property related fee or charge may be imposed or increased, a public hearing upon the proposed fee or charge must be held and a mailed notice sent to the record owner of each identified parcel of land upon which the fee or charge is proposed for imposition. In the public hearing if written protests of the proposed fee or charge are presented by a majority of the owners of affected identified parcel(s), an agency may not impose the fee or charge.

Following the enactment of Proposition 218 in 1996, appellate court cases and an Attorney General opinion initially indicated that fees and charges levied for water and wastewater services are not property-related fees and charges and thus are not subject to the above described requirements of Proposition 218 regarding notice, hearing and protests in connection with any increase in the fees and charges being imposed.

In a decision rendered in February, 2004, the California Supreme Court in *Richmond et al. v. Shasta Community Services District*, 32 Cal. 4th 409, upheld a Court of Appeals decision that water and wastewater connection fees were not property related fees or charges subject to Article XIII D, while at the same time stating in dicta that fees for ongoing water and wastewater service through an existing connection were property related fees and charges.

On March 23, 2005, the California Fifth District Court of Appeal published *Howard Jarvis Taxpayers Association v. City of Fresno*, concluding that in lieu fees charged as a component of water and wastewater utility service charges are subject to the requirements of Proposition 218. The ruling in the *City of Fresno* case relied in part on the *Richmond* decision’s dicta and appeared to conflict with *Apartment Association of Los Angeles County, Inc. v. City of Los Angeles*, 24 Cal. 4th 830 (2001), in which the California Supreme Court ruled that the property-related fee provisions of Proposition 218 apply only to fees triggered by property ownership alone and not by voluntary conduct of the property owner, such as consuming utility services. The *City of Fresno* decision is final, as review has been denied by the California Supreme Court.

On July 24, 2006, the California Supreme Court stated in *Bighorn-Desert View Water Agency v. Beringson* that charges for ongoing water delivery are property related fees and charges within the meaning of Article XIII D and are further subject to the initiative provisions of Section 3 of Article XIII C. This decision reversed the July 2004 California Appellate Court decision (*Bighorn-Desert View Water Agency v. Beringson* (180 Cal. App 4<sup>th</sup> 890)) which opined that the costs of water services are not property related or incidents of property ownership because they are based on consumption and not on property ownership. The California Supreme Court held that such water service charges may be reduced or repealed through a local voter initiative pursuant to Article XIII C of the California Constitution. The Supreme Court stated that it was not holding that the initiative power is free of all limitations and was not determining whether the initiative power is subject to the statutory provision requiring that water service charges be set at a level that will pay debt service on bonded debt and operating expenses. However, the Supreme Court stated in its opinion that water providers may determine rates and charges upon proper action by the governing body and that the legislative body may increase a charge which was not affected by initiative or impose an entirely new charge.

As a result of this case, there can be no assurance that Proposition 218 will not limit the ability of the District to impose, levy, charge and collect increased fees and charges for water services.

On August 24, 2009, the District approved rate increases effective for water usage beginning September 1, 2009 following mailing of notice and a public hearing held pursuant to Article XIII D of the Constitution. This approval includes authorization to raise rates by up to 10% per year for the next five years for costs other than SDCWA and MWD rate increases. The approval includes authorization to pass through all such SDCWA and MWD increases without limitation during the five year period. The Board of Directors will continue to take action each year to set rates, however they are not expected to need to hold another Proposition 218 hearing for three years.

## Taxes

The County levies a 1% *ad valorem* tax on behalf of all taxing agencies in the County, including the District. For Fiscal Year 2010/11, the District's share of such property tax is projected to be \$3.15 million, representing an increase of \$56,000 from amounts received in 2009/10. Such taxes are a source of payment for the Installment Payments. See "SOURCES OF PAYMENT FOR THE BONDS - Installment Payments." All property is assessed using full cash value as defined by Article XIII A of the State Constitution. State law provides exemptions from *ad valorem* property taxation for certain classes of property such as churches, colleges, non-profit hospitals and charitable institutions.

The taxes collected are allocated to taxing agencies within the County, including the District, on the basis of a formula established by State law enacted in 1979 and modified from time to time. Under this formula, the County and all other taxing entities receive a base year allocation plus an allocation on the basis of "situs" growth in assessed value (due to new construction, change of ownership, or a 2% inflation allowance allowed under Article XIII A of the State Constitution) prorated among the jurisdictions which serve the tax rate area within which the growth occurs. Tax rate areas are groups of parcels which are taxed by the same taxing entities. Cities, counties, special districts and school districts share the growth of "base" revenues from each tax rate area. Assessed valuation growth is cumulative, i.e., each year's growth in property value becomes part of each District's allocation in the following year.

Historical assessed valuations for the District may be found in the District's Comprehensive Annual Financial Report, attached hereto as "APPENDIX B." Over the last 30 months, the severe economic recession reverberated through the residential housing market in the County, including many portions of the District and particularly the area in Chula Vista. Between 2008/09 and 2010/11, the assessed valuation of property city-wide in Chula Vista declined 10.4%. The County Assessor reports that the County reduced the value of 225,000 properties throughout the County in 2009, with an average reduction of \$112,000 for a single family home. Foreclosure rates have also increased significantly in the County in the last 36 months. The District's estimate of Taxes for 2010/11 reflects these reduced assessed values.

The availability of revenue from growth in the tax base may be affected by the establishment of redevelopment agencies which, under certain circumstances, may be entitled to revenues resulting from the increase in certain property values. As of the date of this Reoffering Memorandum, a portion of the District's tax base is within a redevelopment plan area.

California law exempts \$7,000 of the assessed valuation of an owner-occupied dwelling but this exemption does not result in any loss of revenue to local agencies since an amount equivalent to the taxes which would have been payable on such exempt values is made up by the State.

Under AB 454 (Statutes of 1987, Chapter 921), the State reports to each county auditor-controller only the county-wide unitary taxable value of State-assessed utility property, without an indication of the distribution of the value among tax rate areas. The provisions of AB 454 apply to all State-assessed property except railroads and non-unitary properties, and do not constitute an elimination of a revision of the method of assessing utilities by the State Board of Equalization. AB 454 allows generally valuation growth or decline of State-assessed unitary property to be shared by all jurisdictions within a county.

From time to time, legislation has been considered as part of the State budget to shift the share of the 1% *ad valorem* property tax collected by counties from special districts to school districts or other governmental entities (the "ERAF Shift"). While legislation enacted in connection with the Fiscal Year 1992/93 State budget shifted approximately 35% of many special districts' shares of the countywide 1% *ad valorem* tax, the share of the countywide 1% *ad valorem* tax pledged to debt service by special districts was exempted. None of the State budgets enacted since Fiscal Year 1992/93 have permanently reallocated additional portions of the special districts' shares of the countywide 1% *ad valorem* tax.

However, the State Budgets for Fiscal Years 2003/04 through 2005/06 reallocated approximately \$1.30 billion of the 1% *ad valorem* property tax from local government to schools. Of that amount, approximately \$350 million was reallocated from special districts. The District estimates that this resulted in a reduction of approximately 40% in Taxes as a result of the ERAF Shift in those years. On July 24, 2009, the California legislature approved amendments to the 2009/10 Budget involving 30 separate pieces of legislation to close a \$26.3 billion shortfall. The Governor signed the budget plan on July 28, 2009. Total State general fund spending in Fiscal Year 2009/10 will be more than \$84 billion, down from nearly \$91.7 billion in Fiscal Year 2008/09 and nearly \$103 billion in Fiscal Year 2007/08. The budget amendments combined deep spending cuts, borrowing from local governments and accounting maneuvers.

The approved amendments included borrowing from local governments and various accounting maneuvers to generate additional revenues in Fiscal Year 2009/10, including (among many others) \$2 billion borrowed from cities, counties and special districts' property tax collections under provisions of Proposition 1A (approved by the voters in 2004), which the State must repay with interest within three years.

The declaration by the State of California of a fiscal emergency under Proposition 1A, as a part of the State's 2009/10 budget adoption, authorized the State to withhold the equivalent of 8% of fiscal 2009/10 property related tax revenues from cities, counties and special districts. The tax revenues are required to be repaid by the State with interest within three years. The District's Proposition 1A receivable was \$267,197. As a part of the budget package, local governments were given the opportunity to sell their Proposition 1A receivable through financing offered by the California Statewide Communities Development Authority, a joint powers authority sponsored by the League of California Cities and California State Association of Counties. California Communities issued bonds in November 2009, securitizing the future payments by the State and remitting the proceeds of the bonds to the local governments who opted to participate in the securitization. The District opted to participate in the securitization program and received all of its Proposition 1A receivable.

There can be no assurance that the share of the 1% *ad valorem* property tax the District currently receives will not be reduced further or deferred or delayed pursuant to State legislation enacted in the future to address future State budget deficits. See "Historical and Projected Taxes, Net Revenues and Debt Service Coverage" herein for historic and projected receipts of Taxes.

## **Personnel**

The District has 156 full-time positions budgeted for Fiscal Year 2011/12. The OWD Employee Association (the "Union") represents 115 of these full-time employees as a collective bargaining unit. The District has not experienced any strikes and continues to have positive labor relations which includes a negotiated five-year Collective Bargaining Agreement that ends on June 30, 2013.

The District provides retirement benefits for its employees through a contractual agreement with the California Public Employees' Retirement System ("CalPERS"). Active members in the District's benefit pension plan are required to contribute 8% of their annual covered salary. The District has elected to contribute 7% on behalf of its employees. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the Fiscal Year ended June 30, 2010 was 19.815%. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. Due to significant investment losses, CalPERS could significantly increase contribution rates over the next several years. For the Fiscal Year ended June 30, 2010, the District's annual pension costs and actual contribution was \$2,240,538, and, for the Fiscal Year ending June 30, 2011, the District's annual pension cost and actual contribution is expected to be \$2,427,744, an 8.4% increase. An increase of 14.3% is expected for 2011/12 and a 2.4% increase is expected for

2012/13. The required contribution for Fiscal Year 2010/11 was determined as part of the June 30, 2008 actuarial valuation, pursuant to which the District had an unfunded actuarial accrued liability of approximately \$15.8 million as of June 30, 2008. As part of the June 30, 2009 actuarial valuation, CalPERS estimates the District's unfunded actuarial accrued liability will not change significantly as of June 30, 2010 or June 30, 2011. Unfunded liabilities are amortized as a level percentage of pay over a closed 20-year period. Gains and losses that occur in the operation of the plan are amortized over a rolling period, which results in an amortization of 10% of unamortized gains and losses each year. If the plan's accrued liability exceeds the actuarial value of plan assets, then the amortization payment of the total unfunded liability may not be lower than the payment calculated over a 30-year amortization period.

In addition to the pension benefits described above, it is the District's practice and policy to provide certain life insurance and health care benefits ("Other Post Employment Benefits, or OPEB") for eligible retired employees, directors and eligible dependents. These benefits vary based on the hire date of the employee. As of the last actuarial projection, dated June 30, 2009, the District's Actuarial Accrued Liability for OPEB benefits was \$10,070,000.

The District has chosen to fund this liability by investing funds with the California Employers' Retiree Benefit Trust Fund (CERBT), an agent multiple-employer plan administered by California Public Employees' Retirement System (CalPERS), which acts as a common investment and administrative agent for participating public employers within the State of California. The District's annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal annual cost. Any unfunded actuarial liability (or funding excess) is amortized over a period not to exceed thirty years. The current ARC rate is 2.3% of the annual covered payroll.

Based on the District's financial statements at June 30, 2010, the amount actually contributed to the CERBT and changes in the District's net OPEB obligation total \$6.8 million. In addition, the District's Board has designated approximately \$3.0 million of its reserves towards the remaining liabilities. In accordance with GASB Statement 45, and the requirements of the CERBT, the District will periodically update the actuarial projections and continue to fund the resulting ARC on an annual basis.

## **Insurance**

### General Liability and Property Damage

The District is exposed to various risks of loss related to torts, theft, damage and destruction of assets, errors and omissions, and natural disasters. Beginning in July 2003, the District began participation in an insurance pool through Special Districts Risk Management Authority (SDRMA). Coverages through SDRMA are as follows: property coverage - \$1 billion/occurrence with replacement cost for scheduled property; \$100 million for boiler and machinery; \$200 million for workers' comp.; \$500,000 for personal liability coverage for board members; \$400,000 for employee dishonesty coverage; \$750,000 for uninsured/underinsured motorists; and \$10 million per occurrence for each of the following types of coverage, auto liability, public officials and employees errors, employment practices liability, employee benefits liability, and general liability.

Separate financial statements for SDRMA may be obtained at: Special District Risk Management Authority, 1112 I Street, Suite 300, Sacramento, California 95814.

### Workers' Compensation

Through SDRMA, the District is insured up to \$200 million Statutory Workers' Compensation and \$5 million in Employer's Liability with a Zero Member Deductible. SDRMA currently has a pool of over 340 agencies in the Workers' Compensation Program.

## Health insurance

Prior to 2008, the District maintained a self-insurance program for health claims. Beginning in January 2008, the District began providing health insurance through SDRMA covering all of its employees, retirees, and other dependents. Prior estimated accrued claims outstanding at June 30, 2008 amounted to \$137,029, and all remaining claims were paid as of December 31, 2008. SDRMA is a self-funded pooled medical program administered in conjunction with the California State Association of Counties (CSAC).

## **District Reserves and Investment Policy**

As of June 30, 2010, the District had approximately \$115.3 million in cash and investments, of which the Board had designated \$52.2 million for capital projects and \$6.6 million for insurance. The District's reserves are not pledged to and do not secure the District's obligation to make Installment Payments.

In accordance with State of California law, the District Board of Directors has approved an investment policy (the "Investment Policy") which complies with Sections 53601 through 53630 of the Government Code of the State of California providing legal authorization for the investment or deposit of funds of local agencies. All investments of the District conform to the restrictions of those laws. The District's investments by category and their respective market value and book value as of March 31, 2011 are set forth in Table 5 below. For additional information relating to the District's investments, see "APPENDIX B - DISTRICT AUDITED FINANCIAL STATEMENTS," Note 2.

**TABLE NO. 6**  
**SUMMARY OF INVESTMENTS**  
**As of March 31, 2011**

<i><u>Investments</u></i>	<i><u>Market Value</u></i>	<i><u>Book Value</u></i>	<i><u>% of Portfolio</u></i>
Federal Agency Issues – Callable	\$66,279,429	\$66,365,240	66.15
Federal Agency Issues – Coupon	-	-	-
Certificates of Deposit – Bank	79,108	79,108	0.07
Local Agency Investment Fund (LAIF)	20,271,906	20,246,352	20.18
San Diego County Pool	12,010,000	11,986,744	11.95

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Source: Olay Water District.

The Investment Policy may be changed at any time at the discretion of the District (subject to the State law provisions relating to authorized investments) and as the California Government Code is amended. Any exception to the Investment Policy must, however, be formally approved by the Board of Directors of the District. There can be no assurance the State law or the Investment Policy will not be amended in the future to allow for investments which are currently not permitted under such State law or the Investment Policy, or that the objectives of the District with respect to investments will not change.

## Outstanding Indebtedness of the District

The District had outstanding indebtedness as of June 30, 2010 as shown in Table No. 7.

TABLE NO. 7  
OTAY WATER DISTRICT  
OUTSTANDING INDEBTEDNESS  
As of June 30, 2010

Category of Indebtedness	Original Issue	Amount Outstanding	Final Maturity
(1) 1996 Certificates of Participation	\$15,400,000	\$11,700,000	2026
(2) 2004 Refunding Certificates of Participation	12,270,000	9,790,000	2023
(3) 2007 Certificates of Participation	42,000,000	40,400,000	2036
(4) 2009 General Obligation Refunding Bonds	7,780,000	7,780,000	2023
(5) State Water Resources Control Board Note	5,000,000	359,744	2011
(6) 2010 Water Revenue Bonds Series A	13,840,000	13,840,000	2025
(6) 2010 Water Revenue Bonds Series B	36,355,000	36,355,000	2041

- (1) In June 1996, the District issued the 1996 Certificates to provide funds for the design, acquisition, construction and equipping of various water and water-related facilities and an administration building for use in connection with the administration of the District. The 1996 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 2004 Certificates, the 2007 Certificates, and the 2010 Bonds. Interest is payable at a variable rate of interest, and the interest rate at April 19, 2011 was 0.26% and was 0.25% at June 30, 2010. At current rates, debt service is expected to be \$400,000 to \$450,000 each year for the next several years. However, the annual installment payments are estimated in the projections at approximately \$980,000 based on the current 25-Year Revenue Bond Index of 4.99%.
- (2) In August 2004, the District issued its 2004 Revenue Refunding Certificates of Participation (the "2004 Certificates") to defease its outstanding 1993 Certificates of Participation. The 2004 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$933,000.
- (3) In March 2007, the District issued its 2007 Revenue Certificates of Participation (the "2007 Certificates") to provide funds for the design, construction and equipping of two 10 million gallon reservoirs and various water-related facilities. The 2007 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$2,501,000.
- (4) Voters within Improvement District No. 27 of the District authorized \$100 million general obligation bonds in 1989. The District issued \$11,500,000 general obligation bonds in 1992 and refinanced the bonds in 1998 and again in 2009. Annual debt service is approximately \$764,000. The District also has approximately \$29 million in general obligation bonds authorized between 1960 and 1978 for various Improvement Districts throughout the District, but unissued. The general obligation bonds are payable from *ad valorem* property tax revenues, which are not a part

of Taxes which secure the Installment Payments. The District has no current plans to issue any of the authorized but unissued general obligation bonds.

- (5) The State Water Resources Control Board Note bears interest at 3.5% and is payable in annual installments of \$366,325. This note has no lien on Net Revenues and Taxes but is payable by the District from any available source.
- (6) In April 2010, Water Revenue Bonds Series 2010A and Water Revenue Bond Series 2010B (Taxable Build America Bonds) (collectively, the “2010 Bonds”) were sold by the Otay Water District Financing Authority to provide funds for the construction of water storage and transmission facilities. The 2010 Bonds are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$3,700,000.

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Source: Otay Water District.

## Historical Operating Results

The following table summarizes the Statement of Net Assets included in the District's audited financial statements for the last five Fiscal Years. The audited financial statements of the District for the Fiscal Year ended June 30, 2010 are attached hereto as "APPENDIX B" and should be read in their entirety.

**TABLE NO. 8  
OTAY WATER DISTRICT  
NET ASSETS  
For the Fiscal Year Ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
<b>ASSETS</b>					
<b>Current Assets:</b>					
Cash and Cash Equivalents	\$ 13,755,907	\$ 8,048,633	\$ 23,351,911	\$ 50,823,237	\$ 40,180,519
Restricted Cash and Cash Equivalents	-	11,191,213	3,753,983	1,760,631	21,131,924
Investments	62,596,513	68,912,864	60,682,507	26,169,080	43,085,300
Restricted Investments	-	19,975,538	-	-	11,150,549
Accounts Receivable	6,808,999	8,675,458	7,689,720	8,029,609	8,959,367
Accrued Interest Receivable	818,798	1,559,081	715,900	319,186	239,355
Taxes and Availability Charges Receivable	-	-	362,976	413,000	366,535
Restricted Taxes and Availability Charges Receivable	318,090	443,854	174,219	190,151	186,813
Inventories	592,426	633,697	711,240	816,865	954,007
Prepaid Expenses and Other Current Assets	<u>664,133</u>	<u>1,164,300</u>	<u>1,908,028</u>	<u>976,045</u>	<u>626,421</u>
Total Current Assets	<u>\$ 85,554,866</u>	<u>\$ 120,604,638</u>	<u>\$ 99,350,484</u>	<u>\$ 89,497,804</u>	<u>\$ 126,880,790</u>
<b>Non-Current Assets:</b>					
<b>Restricted Assets:</b>					
Net OPEB Obligation	\$ -	\$ -	\$ 5,649,008	\$ 6,204,876	\$ 6,783,385
Total Restricted Assets	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,649,008</u>	<u>\$ 6,204,876</u>	<u>\$ 6,783,385</u>
Deferred Bond Issuance Costs	<u>\$ 555,550</u>	<u>\$ 1,254,821</u>	<u>\$ 1,240,166</u>	<u>\$ 1,142,762</u>	<u>\$ 1,703,282</u>
<b>Capital Assets:</b>					
Land	\$ 12,494,062	\$ 12,971,479	\$ 13,025,364	\$ 13,402,840	\$ 13,620,963
Construction in Progress	58,869,241	40,300,055	42,338,220	18,280,278	37,081,849
Capital Assets, Net of Depreciation	<u>325,624,281</u>	<u>370,989,434</u>	<u>391,350,813</u>	<u>422,369,157</u>	<u>420,363,833</u>
Total Capital Assets, Net of Depreciation	<u>\$396,987,584</u>	<u>\$424,260,968</u>	<u>\$446,714,397</u>	<u>\$454,052,275</u>	<u>\$471,066,645</u>
Other Non-Current Assets	<u>283,440</u>	<u>235,694</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total Non-Current Assets	<u>\$397,826,574</u>	<u>\$425,751,483</u>	<u>\$453,603,571</u>	<u>\$461,399,913</u>	<u>\$479,553,312</u>
Total Assets	<u>\$483,381,440</u>	<u>\$546,356,121</u>	<u>\$552,954,055</u>	<u>\$550,897,717</u>	<u>\$606,434,102</u>

Continued on next page.

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**NET ASSETS**  
**For the Fiscal Year Ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
<b>LIABILITIES</b>					
<i>Current Liabilities:</i>					
Current Maturities of Long-term Debt	\$ 4,529,848	\$ 4,519,048	\$ 2,445,214	\$ 2,521,772	\$ 3,668,734
Accounts Payable	11,617,499	10,930,658	13,705,566	11,565,953	15,327,365
Accrued Payroll Liabilities	2,348,851	2,770,958	2,491,182	2,548,731	2,793,408
Other Accrued Liabilities	683,350	1,597,012	1,613,403	444,875	638,015
Customer Deposits	2,489,101	2,622,646	2,719,331	2,806,990	2,146,360
Accrued Interest		-	770,545	706,914	1,154,286
<i>Liabilities Payable From Restricted Assets:</i>					
Accounts Payable	7,633,220	4,492,364	-	-	-
Accrued Interest	413,442	982,858	166,096	153,270	100,326
<b>Total Current Liabilities</b>	<u>\$ 26,715,313</u>	<u>\$ 24,313,374</u>	<u>\$ 17,807,337</u>	<u>\$ 20,748,525</u>	<u>\$ 28,778,494</u>
<i>Non-Current Liabilities:</i>					
<i>Long-term Debt:</i>					
General Obligation Bonds	\$ 8,396,755	\$ 8,045,029	\$ 7,678,302	\$ 7,291,575	\$ 6,763,127
Certificates of Participation	24,119,352	65,051,790	63,192,774	61,468,693	59,694,612
Revenue Bonds					5,253,234
Notes Payable	1,380,778	1,031,710	703,516	350,744	6,010
Other Non-current Liabilities	233,913	890,473	680,709	684,309	684,309
<b>Total Noncurrent Liabilities</b>	<u>\$ 34,600,800</u>	<u>\$ 75,019,022</u>	<u>\$ 72,263,301</u>	<u>\$ 69,804,321</u>	<u>\$ 118,403,282</u>
<b>Total Liabilities</b>	<u>\$ 61,316,113</u>	<u>\$ 99,332,396</u>	<u>\$ 90,070,638</u>	<u>\$ 90,552,846</u>	<u>\$ 147,181,776</u>
<b>NET ASSETS</b>					
Invested in Capital Assets, Net of Related Debt	3,161,590,844	3,174,867,591	3,372,696,591	3,382,410,491	3,377,855,787
Restricted for Net OPEB Asset	-	2,071,307	5,649,008	6,204,876	-
Restricted for Debt Service	-	-	1,762,106	1,797,513	3,192,111
Unrestricted	60,474,482	70,282,627	74,710,712	69,931,092	80,204,428
<b>Total Net Assets</b>	<u>\$ 3,222,065,326</u>	<u>\$ 3,417,021,525</u>	<u>\$ 3,827,827,417</u>	<u>\$ 3,860,744,871</u>	<u>\$ 3,461,252,326</u>

Source: Day Water District Audited Financial Statements

## Historical Debt Service Coverage

Table No. 9 below sets forth historical Taxes and Net Revenues and Debt Service Coverage for the last five Fiscal Years.

**TABLE NO. 9**  
**HISTORICAL TAXES AND NET REVENUES (in '000's) AND DEBT SERVICE COVERAGE**  
**For the Fiscal Year ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
Number of New Connections	884	639	171	141	255
<b>Revenues:</b>					
Water Sales	\$43,756	\$48,606	\$50,809	\$52,399	\$56,210
Connection Fees	1,358	1,540	1,481	1,522	1,908
Other Income	784	874	1,855	1,938	181
Availability Fees <sup>(1)</sup>	558	706	688	575	619
Amusement Fees	1,257	2,120	586	392	556
Capacity Fees	6,715	8,028	1,962	1,851	1,948
Investment Earnings	<u>3,174</u>	<u>4,349</u>	<u>3,947</u>	<u>2,157</u>	<u>1,324</u>
Total Revenue	<u>\$57,602</u>	<u>\$66,223</u>	<u>\$61,268</u>	<u>\$60,834</u>	<u>\$62,746</u>
<b>Operation and Maintenance Costs:</b>					
Water Purchases <sup>(2)</sup>	\$25,460	\$27,494	\$28,187	\$29,310	\$21,818
Utilities	2,114	2,419	2,550	2,842	2,223
Payroll	12,885	17,080	16,488	16,391	16,137
Administrative	4,797	6,136	6,815	6,866	5,181
Materials and Maintenance	<u>2,264</u>	<u>2,365</u>	<u>2,381</u>	<u>1,792</u>	<u>1,706</u>
Total Operation and Maintenance Costs	<u>\$47,520</u>	<u>\$52,474</u>	<u>\$56,421</u>	<u>\$57,201</u>	<u>\$57,085</u>
Net Revenues	\$10,082	\$13,810	\$4,847	\$1,633	\$5,661
Taxes <sup>(3)</sup>	<u>\$ 1,318</u>	<u>\$ 2,930</u>	<u>\$ 3,380</u>	<u>\$ 7,430</u>	<u>\$ 3,009</u>
Taxes and Net Revenues	\$11,400	\$16,740	\$8,227	\$9,063	\$8,670
<b>Debt Service:</b>					
1996 Installment Payments	\$ 760	\$ 757	\$ 651	\$ 542	\$ 580
2004 Installment Payments	948	923	929	928	929
2007 Installment Payments	-	558	1,721	2,491	2,493
2010 Installment Payments	-	-	-	-	518
Letter of Credit Fees	<u>67</u>	<u>66</u>	<u>67</u>	<u>63</u>	<u>129</u>
Total Debt Service	\$ 1,775	\$ 2,304	\$ 3,368	\$ 4,024	\$ 4,649
Coverage Ratio	643%	727%	241%	176%	186%

Source: Otay Water District

<sup>(1)</sup> Includes only water availability charges not exceeding \$10 per acre per year. To the extent such fees over \$10 per acre are authorized for operational purposes, they are included in "Other Income."

<sup>(2)</sup> This District is disputing approximately \$700,000 of water purchase costs charged by the City of San Diego for potable water between July 2006 and January 2008, which have been excluded from the amounts shown above.

<sup>(3)</sup> ERAF Shift reflected in Taxes for Fiscal Year 2005/06. See "THE WATER SYSTEM - Taxes."

## Projected Debt Service Coverage

The projections of Revenues and the corresponding Taxes and Net Revenues shown in Table No. 10 are based on the assumptions shown below. The District believes the assumptions upon which the projections are based are reasonable; however, some assumptions may not materialize and unanticipated events and circumstances may occur (see "RISK FACTORS"). To the extent that the assumptions are not actually realized, the District's ability to timely make the Installment Payments may be adversely affected.

Following is a discussion of assumptions used in the projection of Revenues, Net Revenues and Taxes:

- (a) The District hired MarketPointe Realty Advisors, San Diego, California, to project development of residential and commercial units within the District over the next six years. Based on that forecast, potable connections in equivalent dwelling units are projected to increase as follows for an overall 6.3% increase during the next six year period and recycled connections are also projected to increase 6.7% during the next six year period as follows.

	Potable System		Recycled System	
	<u>Number of Meters (EDU)</u>	<u>% Increase</u>	<u>Number of Meters (EDU)</u>	<u>% Increase</u>
2012	420	0.6%	20	0.5%
2013	605	0.9%	44	1.1%
2014	629	0.9%	47	1.1%
2015	841	1.2%	41	1.0%
2016	896	1.3%	54	1.3%

- (b) Water sales volume (in acre feet) is projected as follows. The District is projecting a 3.1% decrease in potable water sales from originally budgeted amounts for 2010/11 due to conservation efforts, economic conditions and above average rainfall and a 7.7% decrease in recycled water sales from originally budgeted amounts for 2010/11. The District is also projecting some future increases as rainfall returns to normal.

	<u>Potable System</u>	<u>Recycled System</u>	<u>Total</u>
2011	28,267	3,816	32,083
2012	28,946	3,960	32,906
2013	29,452	4,041	33,493
2014	29,976	4,126	34,102
2015	30,333	4,156	34,489
2016	30,712	4,196	34,908

The District receives a credit of \$185 per acre foot and \$200 per acre foot from MWD and SDCWA, respectively, for each acre foot of recycled water. These credits are included in Water Sales revenue.

- (c) Water rates increased 10.9% on January 1, 2011 and are projected to increase 7.7% on January 1, 2012. For the years 2013 and 2014 they are projected to increase by 7.7% annually and in 2015, a 4.9% water rate increase is projected (see "Water Charges – Proposition 218" herein).
- (d) Capacity and annexation fee rates are estimated to increase 3% in each year from existing rates based on the projected Engineering News-Record index increases. Revenue from these fees will also increase as the number of connections increase as shown in (a) above.

- (e) Water availability charges included in Availability Fees are limited to an amount not exceeding \$10 per acre per year. To the extent the water availability charges exceeding \$10 per acre are authorized for operational purposes, such fees are included in Other Income.
- (f) Taxes do not include *ad valorem* taxes levied for the purpose of paying debt service on the District's 1998 General Obligation Refunding Bonds. Taxes are projected to increase slightly for 2011/12 by \$133,000 based on an increase in assessed value, and slowly increase by approximately 2%, annually. No additional ERAF deductions or Proposition 1A borrowings are assumed (see "Taxes" herein).
- (g) Non-operating income is excluded from the projection. Non-operating revenues within "Miscellaneous Revenues" shown in the District's financial statements consist of property rental and golf course income.
- (h) Water Supply costs are anticipated to increase annually as a result of increases in cost of purchased water, effects of changes in weather, and usage by new customers as follows:

2012	8.6%
2013	9.1%
2014	9.6%
2015	8.0%
2016	7.8%

- (i) Operating costs shown in Fiscal Year 2010/11 are based on current year estimates. Costs for subsequent Fiscal Years are based on the 2011/12 estimates with the annual inflationary factors shown below.

Utilities	3.5%
Materials and Maintenance	4.0%
Administrative Costs	3.0%
Salaries	5.1%
Medical Benefits	9.5%
Workers Comp	5.0%
Other Benefits	3.0%

Base operating costs are also increased based on the projected growth in District operations, similar to the growth rates shown for connections in (a) above.

- (j) The debt service on the 1996 Certificates is calculated based on the existing principal repayment schedule and the Bond Buyer 25 Year Revenue Bond Index as of January 27, 2010 of 4.99%. The current letter of credit expires in June 2011. Further annual letter of credit fees are estimated beginning at 85 basis points of the outstanding par amount of the 1996 Certificates, declining to 50 basis points by 2012/13.

**TABLE NO. 10**  
**PROJECTED TAXES AND NET REVENUES (in '000's) AND DEBT SERVICE COVERAGE**  
**For the Fiscal Year ended June 30**

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
<b>Revenues:</b>						
Water Sales	\$ 58,200	\$ 65,304	\$ 71,350	\$ 77,988	\$ 84,162	\$ 89,303
Connection and Other Fees	1,947	1,718	1,813	1,851	1,911	1,954
Availability Fees	601	646	651	660	669	678
Annexation Fees	-	-	-	21	104	196
Capacity Fees	4,589	3,518	3,242	3,489	7,882	8,798
Betterment Fees	677	629	632	638	644	651
Investment Earnings	728	782	993	1,268	1,579	2,167
BABS Subsidy <sup>(1)</sup>	717	830	830	830	830	830
<b>Total Revenue</b>	<b>\$ 65,459</b>	<b>\$ 73,426</b>	<b>\$ 81,513</b>	<b>\$ 88,743</b>	<b>\$ 97,780</b>	<b>\$104,579</b>
<b>Operation and Maintenance Costs:</b>						
Water Purchases	\$ 33,397	\$ 38,244	\$ 41,761	\$ 45,741	\$ 49,402	\$ 53,232
Litigates	2,248	2,359	2,438	2,463	2,578	2,702
Payroll	16,405	17,210	17,788	18,224	18,537	18,807
Administrative	4,183	4,127	4,352	4,469	4,616	4,771
Materials and Maintenance	1,936	2,544	2,853	3,016	3,146	3,282
<b>Total Operation and Maintenance Costs</b>	<b>\$ 58,171</b>	<b>\$ 64,484</b>	<b>\$ 69,042</b>	<b>\$ 73,912</b>	<b>\$ 78,260</b>	<b>\$ 82,793</b>
<b>Net Revenues</b>	<b>\$ 7,288</b>	<b>\$ 8,942</b>	<b>\$ 12,471</b>	<b>\$ 14,831</b>	<b>\$ 19,500</b>	<b>\$ 21,786</b>
<b>Taxes</b>	<b>\$ 3,145</b>	<b>\$ 3,142</b>	<b>\$ 3,142</b>	<b>\$ 3,205</b>	<b>\$ 3,209</b>	<b>\$ 3,433</b>
<b>Taxes and Net Revenues</b>	<b>\$ 10,433</b>	<b>\$ 12,084</b>	<b>\$ 15,613</b>	<b>\$ 18,036</b>	<b>\$ 22,768</b>	<b>\$ 25,220</b>
<b>Debt Service:</b>						
1996 Installment Payments <sup>(2)</sup>	\$ 565	\$ 1,020	\$ 1,134	\$ 1,169	\$ 1,142	\$ 1,209
2004 Installment Payments	928	927	923	922	924	924
2007 Installment Payments	2,497	2,497	2,498	2,497	2,500	2,501
2010 Installment Payments <sup>(1)</sup>	2,548	3,707	3,693	3,675	3,665	3,654
Proposed Debt	-	-	-	-	802	1,022
<b>Total Debt Service</b>	<b>\$ 6,538</b>	<b>\$ 8,151</b>	<b>\$ 8,248</b>	<b>\$ 8,263</b>	<b>\$ 9,033</b>	<b>\$ 9,310</b>
<b>Coverage Ratio <sup>(2)</sup></b>	<b>160%</b>	<b>148%</b>	<b>189%</b>	<b>218%</b>	<b>252%</b>	<b>271%</b>

Source: Gray Water District

<sup>(1)</sup> For the purpose of calculating the coverage ratio, when the 1996 Certificates, 2004 Certificates and 2007 Certificates are no longer outstanding, the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

<sup>(2)</sup> Based on April 14, 2011 25-Year Revenue Bond Index of 5.53% plus letter of credit fees.

The projected Revenues, Taxes and Operation and Maintenance Costs shown above are subject to several variables as described on the previous pages. The District provides no assurance that the projected Taxes and Net Revenues will be achieved (see "RISK FACTORS" herein).

## **RISK FACTORS**

*The following information should be considered by prospective investors in evaluating the 1996 Certificates. However, the following does not purport to be an exhaustive listing of risks and other considerations which may be relevant to investing in the 1996 Certificates. In addition, the order in which the following information is presented is not intended to reflect the relative importance of any such risks.*

### **System Demand**

There can be no assurance that the local demand for service provided by the Water System will increase to levels described in this Official Statement under the heading "THE WATER SYSTEM." Reduction in the level of new connections could require an increase in rates or charges in order to produce Taxes and Net Revenues sufficient to comply with the District's rate covenant in the Installment Purchase Agreement. Such rate increases could increase the likelihood of nonpayment, and could also further decrease demand. Furthermore, there can be no assurance that any other entity with regulatory authority over the Water System will not adopt further restrictions on operation of the Water System.

### **Increased Operation and Maintenance Costs**

There can be no assurance that operation and maintenance costs of the Water System will be consistent with the levels contemplated in this Official Statement. Changes in technology, increases in the cost of operation, increased water treatment requirements or other costs mandated by regulatory agencies or other expenses could require increases in rates or charges in order to comply with the rate covenant described herein and in the Installment Sale Agreement, and could increase the possibility of nonpayment of the 1996 Certificates.

### **Additional Obligations Payable from Taxes and Net Revenues**

The District may issue additional parity obligations or enter into additional Contracts payable from Taxes and Net Revenues on a parity with its pledge of such Taxes and Net Revenues to the Installment Payments relating to the 1996 Certificates and the Existing Parity Obligations. The ability of the District to enter into such Parity Debt is subject to certain requirements set forth in the 1996 Installment Sale Agreement, the 2004 Installment Purchase Agreement, the 2007 Installment Purchase Agreement and the 2010 Installment Purchase Agreement. See "SOURCES OF PAYMENT FOR THE CERTIFICATES - Parity Debt."

The District may also enter into obligations payable from Taxes and Net Revenues which are subordinate to the 1996 Certificates.

### **Risks Relating to Water Supplies**

The District's current potable water supply primarily comes from purchases from SDCWA, which in turn currently purchases approximately 87% of its water supply from MWD and IID. This source of water could become limited due to possible events that include prolonged droughts or similar changes in State-wide weather patterns, earthquakes or other natural disasters, contamination by environmental hazards, or acts of terrorism or civil unrest. There can be no assurance that currently available water supplies would be sufficient to meet demand under current conditions in the event of a prolonged drought or other interruption of the District's source of water supply, or that the District would be able to secure alternate sources of water to meet its customer demand. See "THE WATER SYSTEM - Water Supply" herein for a discussions of the water supply in the region and the District's sources of water in particular.

## **Environmental Regulation**

The kind and degree of water treatment effected through the water system is regulated, to a large extent, by the federal government and the State of California. Treatment standards set forth in federal and state law control the operations of the water system and mandate the use of water treatment technology. If the federal government, acting through the Environmental Protection Agency, or the State of California, acting through the Department of Health Services, or additional federal or state agencies, should impose stricter water quality standards upon the Water System, the District's expenses could increase accordingly and rates and charges would have to be increased to offset those expenses. It is not possible to predict the direction federal or state regulation will take with respect to water quality standards, although it is likely that, over time, both will impose more stringent standards with attendant higher costs.

## **Proposition 218**

On November 5, 1996, California voters approved Proposition 218-Voter Approval for Local Government Taxes-Limitation on Fees, Assessments, and Charges-Initiative Constitutional Amendment. Proposition 218 added Articles XIIC and XIID to the California Constitution, imposing certain vote requirements and other limitations on the imposition of new or increased taxes, assessments and property-related fees and charges. See "THE WATER SYSTEM - Water Charges - Proposition 218" for a discussion of specific issues and risks raised by Proposition 218. The District's current projections assume future rate increases which will be subject to the Proposition 218 notice process.

## **Casualty Risk; Earthquakes**

Any natural disaster or other physical calamity, including earthquake, may have the effect of reducing Revenues and Taxes through damage to the Water System and/or adversely affecting the economy of the surrounding area. The Installment Purchase Agreement requires the District to maintain insurance or self-insurance, but only if and to the extent available at a reasonable cost from reputable insurers, and the District is not expressly required to provide earthquake insurance. The District is located in a seismically active region and structures in the District could be impacted by a major earthquake originating from the numerous faults in the area. Seismic hazards encompass both potential surface rupture and ground shaking. In the event of total loss of the Water System, there can be no assurance that insurance proceeds will be adequate to rebuild the Water System or to redeem all Outstanding 1996 Certificates or that losses in excess of the insured amount will not occur.

## **Early Prepayment Risk**

Early prepayment of the 1996 Certificates may occur in whole or in part without premium, on any date, if the District exercises its right to prepay the 1996 Certificates in whole or in part pursuant to the provisions of the Trust Agreement. Mandatory prepayment of the 1996 Certificates may occur upon the expiration, substitution or termination of the Letter of Credit (see "THE CERTIFICATES - Prepayment").

## **Limited Recourse on Default**

If the District defaults on its obligation to pay the Installment Payments when due, the Trustee, subject to certain rights of the Bank, has the right to accelerate the total unpaid principal amount of the Installment Payments. However, in the event of a default and such acceleration there can be no assurance that the District will have sufficient Taxes and Net Revenues to pay the accelerated principal. Default by the District will not result in loss of the 1996 Project or the Water System or any other assets of the District.

So long as the 1996 Certificates are in book-entry form, DTC (or its nominee) will be the sole registered owner of the 1996 Certificates, and the rights and remedies of the Certificate Owners will be exercised through the procedures of DTC.

## **Bankruptcy Risks**

The enforceability of the rights and remedies of the owners of the 1996 Certificates and the obligations of the District may become subject to the following: the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditors' rights generally, now or hereafter in effect; usual equitable principles which may limit the specific enforcement under state law of certain remedies: the exercise by the United States of America of the powers delegated to it by the federal Constitution; and the reasonable and necessary exercise, in certain exceptional situations of the police power inherent in the sovereignty of the State of California and its governmental bodies in the interest of servicing a significant and legitimate public purpose. Bankruptcy proceedings, or the exercise of powers by the federal or state government, if initiated, could subject the owners of the 1996 Certificates to judicial discretion and interpretation of their rights in bankruptcy or otherwise and consequently may entail risks of delay, limitation, or modification of their rights.

## **No Obligation to Tax**

The obligation of the District to pay Installment Payments does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation, except the Taxes. The obligation of the District to pay Installment Payments does not constitute a debt or indebtedness of the District, the State of California or any of its political subdivisions, within the meaning of any constitutional or statutory debt limitation or restriction.

## **Change in Law**

In addition to the other limitations described herein, the California electorate or Legislature could adopt a constitutional or legislative initiative with the effect of reducing revenues payable to or collected by the District. There is no assurance that the California electorate or Legislature will not at some future time approve additional limitations that could have the effect of reducing the Taxes and Net Revenues and adversely affecting the security of the 1996 Certificates.

## **Loss of Tax Exemption**

In order to maintain the exclusion from gross income for federal income tax purposes of the interest on the 1996 Certificates, the District has covenanted in the Installment Sale Agreement to comply with each applicable requirement of Section 103 and Sections 141 through 150 of the Internal Revenue Code. The interest on the 1996 Certificates could become includable in gross income for purposes of federal income taxation retroactive to the date of execution and delivery of the 1996 Certificates, as a result of acts or omissions of the District in violation of this or other covenants in the Installment Sale Agreement or the Trust Agreement. Should such an event of taxability occur, the 1996 Certificates are not subject to prepayment or any increase in interest rates and will remain outstanding until maturity or until prepaid under one of the redemption provisions contained in the Trust Agreement. See "LEGAL MATTERS - Tax Matters" herein.

## **Risks Relating to Build America Bonds Interest Subsidy**

The District must comply with certain requirements of the Code in order for the 2010B Bonds to be treated as qualified bonds and to continue to be eligible for the Interest Subsidy Payment. The District has covenanted to comply with each of these requirements. However, failure by the District to comply with these requirements may result in a delay or forfeiture of all or a portion of the Interest Subsidy Payment and may cause the 2010B Bonds to cease to be treated as qualified bonds either prospectively from the date of determination of a failure to comply with the requirements or retroactively to the date of execution and delivery of the 2010B Bonds. Should such an event occur, the 2010B Bonds are subject to

extraordinary prepayment. If the District is obligated to provide for the issuance of refunding obligations in order to redeem the 2010B Bonds prior to their maturity, the District would be subject to the various risks attendant to issuance of refunding obligations, including higher-than-desired interest rates and duplicative transaction costs. In addition, it is important to note that Build America Bonds are a new product introduced by the American Recovery and Reinvestment Act, which was signed into law on February 17, 2009. The Interest Subsidy Payments do not constitute a full faith and credit guarantee of the United States government, but are required to be paid by the Treasury under the American Recovery and Reinvestment Act. As such, the District can provide no assurance that future legislation or clarifications or amendments to the Code, if enacted into law, or future court decisions will not reduce or eliminate the Interest Subsidy Payment with respect to the 2010B Bonds. The Treasury may offset any Interest Subsidy Payments to which the Otay Water District Financing Authority (the "Authority") is otherwise entitled against any other tax liability of the Authority payable to the Treasury, such as withholding or payroll taxes, or other penalties or interest that may be owed at any time to the Treasury. The District is obligated under the 2010 Installment Purchase Agreement for the 2010 Bonds to make those installment payments without regard to the receipt or deposit of Interest Subsidy Payments. If the Interest Subsidy is delayed or forfeited, it will cause a reduction in Net Revenues available to pay Installment Payments and payments due with respect to the Existing Parity Obligations.

## **LEGAL MATTERS**

### **Enforceability of Remedies**

The remedies available to the Trustee and the Owners of the 1996 Certificates upon an event of default under the Trust Agreement, the Installment Sale Agreement or any other document described herein are in many respects dependent upon regulatory and judicial actions which are often subject to discretion and delay. Under existing law and judicial decisions, the remedies provided for under such documents may not be readily available or may be limited. The various legal opinions to be delivered concurrently with the delivery of the 1996 Certificates will be qualified to the extent that the enforceability of certain legal rights related to the Trust Agreement and Installment Sale Agreement are subject to limitations imposed by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally and by equitable remedies and proceedings generally.

### **Approval of Legal Proceedings**

Certain legal matters related to this Reoffering Memorandum will be passed upon by Best Best & Krieger LLP, as Special Counsel, for the District by its General Counsel and by Stradling Yocca Carlson & Rauth, a Professional Corporation, and for the Bank by its counsel, Musick, Peeler and Garrett, LLP. The Series 1995 Bonds are available for delivery through the DTC book-entry system.

### **Tax Matters**

#### **Original Opinion**

On June 18, 1996, Best Best & Krieger LLP, Special Counsel to the District in connection with the execution and delivery of the 1996 Certificates, delivered their opinion to the effect that, based upon an analysis of then existing statutes, regulations, rulings and judicial decisions, and assuming, among other matters, compliance with certain covenants and requirements, the interest component of the Installment Payments made by the District under the Installment Sale Agreement and received by the Certificate Owners was excluded from gross income for federal income tax purposes, was not an item of tax preference for purposes of federal individual or corporate alternative minimum tax, but such interest component may be included in the calculation of corporation alternative minimum taxable income, and such interest component is exempt from State of California personal income taxes. A complete copy of

the opinion of Special Counsel delivered at the original execution and delivery of the 1996 Certificates is set forth in "APPENDIX D" hereto.

### **No Updated Special Counsel Opinion**

Special Counsel has not taken, and does not intend to take, any action to update their original opinions or to determine if the interest component of the Installment Payments is presently excluded from gross income for federal income tax purposes or exempt from State of California personal income taxes.

### **General Considerations**

Notwithstanding the foregoing, investors should be aware of the following information.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the interest component of the Installment Payments relating to the 1996 Certificates. The District has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that the interest component of the Installment Payments relating to the 1996 Certificates will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in the interest component of the Installment Payments relating to the 1996 Certificates being included in gross income for federal income tax purposes, possibly from the date of original issuance of the 1996 Certificates. The opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates assumed the accuracy of these representations and compliance with these covenants. Special Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Special Counsel's attention after the date of execution and delivery of the 1996 Certificates may adversely affect the value of, or the tax status of interest with respect to, the 1996 Certificates. Accordingly, the opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates is not intended to, and may not, be relied upon in connection with any such actions, events or matters.

Although Special Counsel has rendered an opinion that interest component of the Installment Payments relating to the 1996 Certificates is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest with respect to, the 1996 Certificates may otherwise affect a Beneficial Owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial Owner or the Beneficial Owner's other items of income or deduction. Special Counsel express no opinion regarding any such other tax consequences.

Future legislative proposals, if enacted into law, clarification of the Code or court decisions may cause interest component of the Installment Payments relating to the 1996 Certificates to be subject, directly or indirectly, to federal income taxation or to be subject to or exempted from state income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislative proposals, clarification of the Code or court decisions may also affect the market price for, or marketability of, the 1996 Certificates. Prospective purchasers of the remarketed 1996 Certificates should consult their own tax advisors regarding any pending or proposed federal or state tax legislation, regulations or litigation, as to which Special Counsel expresses no opinion.

The opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates was based on current legal authority existing as of June 18, 1996, covered certain matters not directly addressed by such authorities, and represented Special Counsel's judgment as to the proper treatment of the 1996 Certificates for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Special Counsel cannot give and has not given any opinion or assurance about the future activities of the District, or about the effect of future changes in the

Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The District has covenanted, however, to comply with the requirements of the Code.

Special Counsel's engagement with respect to the 1996 Certificates ended on June 18, 1996 with the original execution and delivery of the 1996 Certificates. Unless separately engaged, Special Counsel is not obligated to defend the District or the Beneficial Owners regarding the tax-exempt status of the interest component of the Installment Payments relating to the 1996 Certificates in the event of an audit examination by the IRS. Under current procedures, parties other than the District and their appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the District legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the 1996 Certificates for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the 1996 Certificates and may cause the District or the Beneficial Owners to incur significant expense.

## **Litigation**

There is no action, suit or proceeding known to be pending or threatened, restraining or enjoining the District in the execution or delivery of, or in any way contesting or affecting the validity of, the 1996 Certificates. There is no litigation known to be pending, or to the knowledge of the District, threatened, questioning the existence of the District or the title of the officers of the District to their respective offices.

There exist lawsuits and claims against the District, which are incidental to the ordinary course of operations of the District's water system and related activities. In the view of the District's management and of the General Counsel to the District, there is no litigation, present or pending, which will individually or in the aggregate materially impair the District's ability to service its indebtedness or which will have a material adverse effect on the business operations of the District.

## **CONCLUDING INFORMATION**

### **Rating on the Certificates**

In connection with this Reoffering Memorandum, it is expected that Standard & Poor's Ratings Services ("S&P") will assign the 1996 Certificates the rating of "A-1/A+", with the understanding that the Letter of Credit will be issued by the Bank on June 30, 2011. The rating should be evaluated independently of any other rating of the District. No application has been made to any other rating agency in order to obtain additional ratings on the 1996 Certificates. The credit enhanced rating on the 1996 Certificates reflect the S&P's current assessment of the creditworthiness of the Bank and its ability to pay draws under the Letter of Credit. Any further explanation as to the significance of the above rating may be obtained from S&P.

The above described rating is not recommendations to buy, sell or hold the 1996 Certificates, and such rating may be subject to revision or withdrawal at any time by S&P. Neither the District nor the Remarketing Agent undertake any responsibility either to bring to the attention of the owners of the 1996 Certificates the downward revision or withdrawal of any rating obtained or to oppose any such revision or withdrawal. Any downward revision or withdrawal of the rating may have an adverse effect on the market price of the 1996 Certificates.

## **Remarketing Agent**

J.P. Morgan Securities LLC serves as Remarketing Agent for the 1996 Certificates. The Remarketing Agent will carry out the duties and obligations provided for the Remarketing Agent under and in accordance with the provisions of the Trust Agreement and the Remarketing Agreement, by and between the District and the Remarketing Agent, dated as of June 1, 1996. The principal office of the Remarketing Agent (for purposes of its responsibilities as Remarketing Agent) is New York, New York.

## **Additional Information**

The summaries and references contained herein with respect to the Trust Agreement, the Installment Sale Agreement, the 1996 Certificates, statutes and other documents, do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute and references to the 1996 Certificates are qualified in their entirety by reference to the form thereof included in the Trust Agreement. Definitions of certain terms used herein are set forth in "APPENDIX A." Copies of the Trust Agreement and the Installment Sale Agreement are available for inspection from the District, 2554 Sweetwater Springs Blvd., Spring Valley, California 91978.

## **References**

Any statements in this Reoffering Memorandum involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Reoffering Memorandum is not to be construed as a contract or agreement between the District and the purchasers or Owners of any of the 1996 Certificates.

## **Execution**

The execution of this Reoffering Memorandum has been duly authorized by the Otay Water District.

### **OTAY WATER DISTRICT**

By: \_\_\_\_\_  
General Manager

## APPENDIX A

### SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The following is a summary of certain provisions of the Installment Sale Agreement and the Trust Agreement which are not described elsewhere in the Official Statement. These summaries do not purport to be comprehensive and reference should be made to the Installment Sale Agreement and the Trust Agreement for a full and complete statement of their respective provisions. All capitalized terms used and not defined in the Official Statement have the meanings set forth in the Installment Sale Agreement or the Trust Agreement.

Unless the context otherwise requires, the terms defined under this caption will for all purposes of the Official Statement have the meanings herein specified.

“Accountant’s Report” means a report signed by an Independent Certified Public Accountant.

“Additional Costs” shall mean those costs the District is required to pay as more particularly set forth in the Installment Sale Agreement.

“Agreement” or “Installment Sale Agreement” means the Installment Sale Agreement as originally executed or as it may be from time to time amended as provided for therein, including as amended by the First Supplement to Installment Sale Agreement.

“Authorized Denomination” means (i) while the Certificates bear interest at a Daily, Weekly, Monthly or CP Rate, \$100,000, and (ii) while the Certificates bear interest at a Tender or Fixed Rate, \$5,000, and in all cases, whole multiples thereof; provided that one or more Certificates may be in a denomination less than \$100,000 while the Certificates bear interest of a Daily, Weekly, Monthly or CP rate in order to match sinking fund installments set forth in the Trust Agreement.

“Bank” means Union Bank, N.A., as issuer of the Facility, until a Substitute Facility is issued and effective in accordance with the Trust Agreement, and thereafter “Bank” shall mean the obligor on such Substitute Facility. If the Facility is provided by more than one financial institution or insurance company as permitted by the Trust Agreement the term “Bank” shall be modified as necessary as permitted by the Trust Agreement.

“Bank Certificates” means Certificates purchased with amounts drawn on the Facility pursuant to the Trust Agreement and owned by and registered to the Bank or its nominee or transferee.

“Bank Rate” means the rate or rates per annum payable with respect to each Bank Certificate, which shall be as provided in the Reimbursement Agreement dated as of June 30, 2011 by and between the Bank, the Corporation and the District relating to the Letter of Credit, or, in the event that a Substitute Facility is in effect, as may be provided in such other agreement relating to such Substitute Facility as may be applicable thereto, provided that such rate shall not exceed the maximum rate permitted by applicable law.

“Business Day” means any day of the year other than Saturday or Sunday on which banks in New York, New York, and in Los Angeles, California and any other city in which the principal office of the Bank may be located are not authorized or required by law or executive order to close and on which the New York Stock Exchange is not closed.

“Certificate Payment Fund” means the fund by that name established in the Trust Agreement.

“Certificate Year” means the period beginning on the date of execution and delivery of the Certificates and ending on September 1, 1996, and each successive one-year or shorter period thereafter beginning on September 2 and ending on September 1 until there are no Outstanding Certificates.

“Code” means the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder.

“Debt Service Account” means the account by that name established pursuant to the Trust Agreement.

“Default Rate” shall have the meaning as set forth in the Reimbursement Agreement.

“District Payments Account” means the accounts by that name established pursuant to the Trust Agreement.

“Eligible Funds” means:

(a) Certificate proceeds deposited with the Trustee contemporaneously with the delivery and sale of the Certificates (other than proceeds of sale of Certificates to the District) and which were continuously thereafter subject to the lien of the Trust Agreement in a separate and segregated fund, account or subaccount established hereunder in which no moneys which were not Eligible Funds were at any time held, together with the investment earnings thereon;

(b) Moneys (i) held in any fund, account or subaccount established hereunder in which no other moneys which are not Eligible Funds are held, and (ii) which have been on deposit with the Trustee for at least three hundred sixty-seven (367) consecutive days during which period no Event of Bankruptcy shall have occurred, together with the investment earnings thereon;

(c) Proceeds of a drawing under the Facility and interest earned on such proceeds; and

(d) Proceeds from the issuance and sale of refunding bonds or other evidence of indebtedness and interest earned on such proceeds and any other moneys deposited with the Trustee if there is delivered to the Trustee at the time of the issuance and sale of such refunding bonds or other evidence of indebtedness or the deposit of such other moneys with the Trustee a written opinion of counsel acceptable to the Rating Agency experienced in bankruptcy matters to the effect that payments with such proceeds or other moneys, as the case may be, of principal of, premium, if any, or interest on the Bonds would not be avoidable as avoidable transfers under the United States Bankruptcy Code should an Event of Bankruptcy hereafter occur.

“Event of Bankruptcy” means the filing of a petition in bankruptcy or the commencement of a proceeding under the United States Bankruptcy Code pursuant to Sections 301 or 303 thereof by or against the District.

“Event of Default” means an event of default under the Installment Sale Agreement, and an event of default under the Trust Agreement.

“Facility” means the Letter of Credit and any Substitute Facility.

“Federal Securities” means any of the following which are noncallable and which at the time of investment are legal investments under the laws of the State of California, as shall be certified in writing by the District to the Trustee, for the moneys proposed to be invested therein:

(a) direct general obligations of (including obligations issued or held in book entry form on the books of the Department of the Treasury of the United States of America), or obligations the payment of principal of and interest on which are directly or indirectly unconditionally guaranteed by, the United States of America; and

(b) direct obligations of any department, agency or instrumentality of the United States of America the timely payment of principal of and interest on which are fully guaranteed by the United States of America.

“First Supplement to Installment Sale Agreement” means the First Supplement to Installment Sale Agreement by and between the Corporation, the District and the Trustee, dated as of June 1, 2011.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the last day of June of the following calendar year, or any other twelve-month period selected and designated as the official Fiscal Year of the District.

“Fixed Rate Conversion Date” means a Conversion Date with respect to a Fixed Rate.

“Gross Revenues” means (i) all water availability charges imposed pursuant to Chapter 2 of Part 5 of the Law not exceeding \$10 per acre per year; (ii) all income, rents, rates, fees, charges and other moneys derived by the District from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (a) all income, rents, rates, fees, charges or other moneys derived from the sale, furnishing, and supplying of water and other services, facilities and commodities sold, furnished or supplied through the facilities of the Water System, including connection fees, (b) the earnings on and income derived from the investment of such income, rents, rates, fees and charges or other moneys, and (c) the proceeds derived by the District directly or indirectly from the sale, lease or other disposition of a part of the Water System as permitted hereunder: provided that the term “Gross Revenues” shall not include customers’ deposits or any other deposits subject to refund until such deposits have become the property of the District.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants appointed by the District, who has a favorable reputation in the field in which its opinion or certified will be given, and:

- (a) is in fact independent and not under domination of the District;
- (b) does not have any substantial interest, direct or indirect, with the District; and
- (c) is not connected with the District as an officer or employee of the District, but who may be regularly retained to make reports to the District.

“Independent Financial Consultant” means a firm of certified public accountants or a consulting engineering firm or engineer, of favorable national or regional reputation, which is not an employee of, or otherwise controlled by, the Corporation, the Trustee or the District.

“Information Services” means the Electronic Municipal Market Access website of the Municipal Securities Rulemaking Board.

“Installment Payment Date” means (1) each date upon which principal component payments are due and payable as set forth on in the Installment Sale Agreement, and (2) each Interest Payment Date.

“Installment Payment Fund” means that fund by that name established pursuant to the Installment Sale Agreement.

“Installments” or “Installment Payments” means the installment payments payable by District pursuant to the Installment Sale Agreement during the Term.

“Interest Payment Date” means:

(a) When the Certificates represent interest at the Daily, Weekly or Monthly Rate, the first Business Day of each calendar month except with respect to the first Interest Payment Date after the Delivery Date which shall be August 1, 2011;

(b) When the Certificates represent interest at a CP Rate, the first Business day immediately following the last day of each CP Rate Period applicable thereto;

(c) When the Certificates represent interest at the Fixed Rate, the first day of each March and September; and

(d) For the Certificates which are subject to mandatory tender pursuant to the Trust Agreement, the date of the mandatory tender (regardless of whether a Holder elects to retain any such Certificates on such date).

“Management Consultant” means any Person of national reputation qualified to report on questions relating to the financial condition of health care facilities, selected by the District, and who (i) is in fact independent of and not under the control of the District, (ii) does not have any substantial interest direct or indirect in the District, and (iii) is not connected with the District as a director, officer or employee of the District, but who may be regularly retained by the District to make annual or other regular reports to the District.

“Maximum Interest Rate” means the lesser of 12% or the maximum amount permitted by State of California law.

“Minimum Permitted Investment Rating” means a rating of “Aa” or better by Moody’s Investors Service or “AA” or better by Standard & Poor’s Ratings Group or “AA” or better by Fitch Investors Service, Inc. or “A” or better by A.M. Best and Company, determined without regard to whether such rating is qualified by a conditional or provisional modifier.

“Moody’s” means Moody’s Investors Service, 99 Church Street, New York, New York 10007, a corporation organized and existing under the laws of the State of Delaware, except that if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, then the term “Moody’s” shall be deemed to refer to any other nationally recognized securities rating agency selected by the District upon written notice to the Trustee and the Bank.

“Net Proceeds” means any insurance or condemnation award paid with respect to the Project, or any proceeds resulting from the sale of any or all portions of the Project remaining after payment therefrom of all expenses incurred in the collection thereof.

“Net Revenues” means Gross Revenues less Operation and Maintenance Expenses.

“Operation and Maintenance Expenses” means all expenses and costs of management, operation, maintenance and repair of the Water System, and all incidental costs, fees and expenses properly chargeable to the Water System and any rebate to the United States Government pursuant to the Code (but excluding debt service or other similar payments on Parity Debt or other obligations and depreciation and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature), all as determined in accordance with generally accepted accounting practices.

“Opinion of Bond Counsel” means a written opinion of nationally recognized bond counsel (who may be counsel for the District) acceptable to the District and the Trustee to the effect that the action proposed to be taken is authorized or permitted by the laws of the State, the Trust Agreement and the Installment Sale Agreement and will not adversely affect the validity of the Installment Sale Agreement or the Certificates under the laws of the State or the exclusion from gross income for federal income tax purposes of interest with respect to the Certificates.

“Outstanding,” when used as of any particular time with reference to Certificates or Parity Debt, means all Certificates and Parity Debt except --

- (1) Certificates (or portions of Certificates) or Parity Debt canceled by the Trustee or delivered to the Trustee for cancellation;
- (2) Certificates (or portions of Certificates) or Parity Debt (or portions of Parity Debt) paid or deemed to have been paid within the meaning defined in the Trust Agreement;
- (3) Certificates or Parity Debt in lieu of or in substitution for which other Certificates or Parity Debt shall have been executed and delivered by the Trustee pursuant to the Trust Agreement; and
- (4) Untendered Certificates.

“Owner” or “Holder” or “Certificate Owner” or “Certificate Holder” or “Owner of Certificates” or “Holder of Certificates” or any similar term, when used with respect to the Certificates, means any person who shall be the registered owner of any Outstanding Certificate. “Owner” or “Holder” or “Certificate Owner” or “Certificate Holder” or “Owner of Certificates” or “Holder of Certificates” shall mean the Bank or the nominee of the Bank with respect to any Bank Certificates.

“Parity Debt” means the 2004 Certificates, the 2007 Certificates and the 2010 Bonds and indebtedness or other obligations (including leases and installment sale agreements) issued or incurred by the District and secured by a pledge of and lien on Taxes and/or Net Revenues equally and ratably with the Installment Payments.

“Permitted Investments” means any of the following which at the time of investment are legal investments under the laws of the State of California for the moneys proposed to be invested therein:

- (1) Federal Securities;
- (2) direct obligations of the United States of America and securities fully and unconditionally guaranteed as to the timely payment of principal and interest by the United States of America; provided, that the full faith and credit of the United States of America must be pledged to any such direct obligation or guarantee (“Direct Obligations”);
- (3) direct obligations and fully guaranteed certificates of beneficial interest of the Export-Import Bank of the United States; consolidated debt obligations and letter of credit-backed issues of the Federal Home Loan Banks; participation certificates and senior debt obligations of the Federal Home Loan Mortgage Corporation (“FHLMCs”); debentures of the Federal Housing Administration; mortgage-backed securities (except stripped mortgage securities which are valued greater than par on the portion of unpaid principal) and senior debt obligations of the Federal National Mortgage Association (“FNMA’s”); participation certificates of the General Services Administration; guaranteed mortgage-backed securities and guaranteed participation certificates of the Government National Mortgage Association (“GNMA’s”); guaranteed participation certificates and guaranteed pool certificates of the Small Business Administration; debt obligations and letter of credit-backed issues of the Student Loan Marketing Association; local authority

bonds of the U.S. Department of Housing & Urban Development; guaranteed Title XI financings of the U.S. Maritime Administration; guaranteed transit bonds of the Washington Metropolitan Area Transit Authority; Resolution Funding Corporation securities;

- (4) direct obligations of any state of the United States of America or any subdivision or agency thereof whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "A" or better by Moody's and "A" or better by S&P or any obligation fully and unconditionally guaranteed by any state, subdivision or agency whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "A" or better by Moody's and "A" or better by S&P;
- (5) commercial paper (having original maturities of not more than 270 days) rated, at the time of purchase, "P-1" by Moody's and "A-1" or better by S&P;
- (6) federal funds, unsecured certificates of deposit, time deposits or bankers acceptances (in each case having maturities of not more than 365 days) of any domestic bank including a branch office of a foreign bank which branch office is located in the United States, provided legal opinions are received to the effect that full and timely payment of such deposit or similar obligation is enforceable against the principal office or any branch of such bank, which, at the time of purchase, has a short-term "Bank Deposit" rating of "P-1" by Moody's and a "Short-Term CD" rating of "A-1" or better by S&P;
- (7) deposits of any bank or savings and loan association which has combined capital, surplus and undivided profits of not less than \$3,000,000, provided such deposits are continuously and fully insured by the Bank Insurance Fund or the Savings Association Insurance Fund of the Federal Deposit Insurance Corporation, including deposits of the Trustee or any of its affiliates;
- (8) investments in money-market funds rated "AAAm" or "AAAm-G" by S&P and at least "AA" by Moody's including any such funds advised by or of the Trustee or an affiliate;
- (9) repurchase agreements collateralized by Direct Obligations, GNMA's, FNMA's or FHLMC's with any registered broker/dealer subject to the Securities Investors' Protection Corporation jurisdiction or any commercial bank insured by the FDIC, if such broker/dealer or bank has an uninsured, unsecured and unguaranteed obligation rated "P-1" or "A3" or better by Moody's and "A-1" or "A-" or better by S&P, provided:
  - (a) a master repurchase agreement or specific written repurchase agreement governs the transaction; and
  - (b) the securities are held free and clear of any lien by the Trustee or an independent third party acting solely as agent for the Trustee. and such third party is (i) a Federal Reserve Bank, (ii) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$50,000,000, or (iii) a bank approved in writing for such purpose by the Bank and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee; and
  - (c) a perfected first security interest under the Uniform Commercial Code, or book-entry procedures prescribed at 31 C.F.R. 306.1 et seq. or 31 C.F.R. 350.0 et seq. in such securities is created for the benefit of the Trustee; and

- (d) the repurchase agreement has a term of 180 days or less, and the Trustee or the Agent will value the collateral securities no less frequently than weekly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within two Business Days of such valuation; and
- (e) the fair market value of the securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 103%;
- (10) the Local Agency Investment Fund maintained by the Treasurer of the State of California;
- (11) any investment agreement or similar investment arrangement with a financial institution, the long-term unsecured obligations of which are rated “AA” or better by Moody’s and S&P, by the terms of which the Trustee is required to withdraw all amounts invested therein if such rating falls below “AA”; and
- (12) pre-refunded municipal obligations defined as follows: Any bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on the date specified in the notice; and (A) which are rated, based on the escrow, in the highest rating category of S&P and Moody’s or any successors thereto; or (B)(i) which are fully secured as to principal and interest and prepayment premium, if any, by a fund consisting only of cash or noncallable Federal Securities, which fund may be applied only to the payment of such principal of and interest and prepayment premium, if any, on such bonds or other obligations on the maturity date or dates thereof or the specified prepayment date or dates pursuant to such irrevocable instructions, as appropriate, and (ii) which fund is sufficient, as verified by an Independent Certified Public Accountant, to pay principal of and interest and prepayment premium, if any, on the bonds or other obligations described in this paragraph on the maturity date or dates thereof or on the prepayment date or dates specified in the irrevocable instructions referred to above, as appropriate.

“Prepayment Account” means the account by that name established in the Trust Agreement.

“Prepayment Price” means, with respect to any Certificate (or portion thereof), the principal amount with respect to such Certificate (or portion thereof) plus the applicable premium, if any, payable upon prepayment thereof pursuant to the provisions of such Certificate and the Trust Agreement.

“Priority Debt” means indebtedness or other obligations (including other leases and installment sale agreements) issued and incurred by the District and secured by a pledge of and lien on Taxes and/or Net Revenues which is senior to and has priority over the pledge of and lien on Taxes and/or Net Revenues securing payment of the Installment Payments.

“Project” means the public improvements acquired and constructed or to be acquired and constructed by the District with the proceeds of the Certificates, each as more particularly described in the Installment Sale Agreement, or any property substituted therefor in conformance with the Installment Sale Agreement.

“Purchase Date” means the date upon which the Tender Agent is obligated to purchase a Certificate or Certificates pursuant to the Trust Agreement.

“Purchase Price” of any Certificate required to be purchased by the Tender Agent pursuant to the Trust Agreement means an amount equal to the principal amount of such Certificate plus, if the Purchase Date is other than an Interest Payment Date, accrued interest thereon, at the rate applicable to the Certificates from the most recent Interest Payment Date and up to but excluding the Purchase Date.

“Project Purchase Price” means the amount determined pursuant to the Installment Sale Agreement.

“Rating Agencies” means Moody’s and S&P.

“Rebate Fund” means the fund by that name established in the Trust Agreement.

“Record Date” means for the interest payable on any Interest Payment Date means (i) the Business Day immediately prior to the Interest Payment Date in question in the case of the Daily and Weekly Rate Periods, (ii) the last Business Day at least five (5) days prior to the Interest Payment Date in question in the case of the Monthly or CP Rate Periods, and (iii) the 15<sup>th</sup> day (whether or not a Business Day) of the calendar month immediately preceding such Interest Payment Date in the case of a Fixed Rate Period.

“Registrar” means the Trustee or such other entity as the Trustee or the District may designate to act as registrar for the Certificates pursuant to the Trust Agreement.

“Related Documents” means the Trust Agreement, the Facility, the Installment Sale Agreement, the Certificates, the Remarketing Agreement, the Official Statement, the Reoffering Memorandum and any other document or instrument required or stated to be delivered hereunder or thereunder on the Delivery Date.

“Remarketing Agent” means J.P. Morgan Securities LLC, in its capacity as successor remarketing agent for the Certificates, or any successor entity appointed by the District and approved by the Bank to perform the duties of the Remarketing Agent hereunder.

“Remarketing Agreement” means the Remarketing Agreement dated as of June 1, 1996, by and between the District and the Remarketing Agent as amended.

“Reserve Credit Facility” means a policy of insurance, a surety bond, a letter of credit or other comparable credit facility, or a combination thereof, which, together with money on deposit in the reserve fund, if any, provide an aggregate amount equal to the Reserve Requirement, so long as the provider of any such policy of insurance, surety bond, letter of credit or other comparable credit facility is rated in the highest rating category by Standard & Poor’s Ratings Group, Moody’s Investors Service or A.M. Best & Company.

“Responsible Officer” means any officer of the Trustee assigned to administer its duties under the Trust Agreement.

“Revenue Fund” means the fund by that name established pursuant to the Installment Sale Agreement.

“Securities Depositories” means: The Depository Trust Company, 711 Stewart Avenue, Garden City, New York 11530, Fax (516) 227-4039 or 4190: and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses as such depositories may specify and/or such other securities depositories as the District may designate in a Written Request of the District delivered to the Trustee.

“Special Counsel” or “Bond Counsel” means Best Best & Krieger LLP, or a firm of nationally recognized attorneys experienced in the issuance of obligations the interest on which is excluded from gross income for purposes of Section 103 of the Code, which firm is selected by the District.

“S&P” means Standard & Poor’s Ratings Group, a corporation organized and existing under and pursuant to the laws of the State of New York, and its successors and assigns, except that if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, then the term “S&P” shall be deemed to refer to any other nationally recognized securities rating agency selected by the District upon written notice to the Trustee and the Bank.

“State” means the State of California.

“Stated Amount” means the maximum aggregate amount available to be drawn under the Facility, which initially shall be \$15,572,142.47 as from time to time decreased and/or increased in accordance with the term of the Facility.

“Stated Maturity” when used with respect to any Certificate or any installment of interest thereon means the date specified in such Certificate as the fixed date on which the principal of such Certificate or such installment of interest is due and payable.

“Statement of the District or the Corporation” means, as applicable, a statement signed by or on behalf of (i) the Corporation by its President or a Vice President, or (ii) by the District by the Chairman of its Board of Directors or General Manager or by any other person who is specifically authorized by resolution of the Board of Directors of the District to sign or execute such a document on its behalf. If and to the extent required by the provisions of the Trust Agreement, each Statement of the Corporation or District shall include the statements provided for in the Trust Agreement.

“Substitute Facility” means a facility meeting the requirements set forth in the Trust Agreement.

“Tax Revenue Fund” means the fund by that name established under the Installment Sale Agreement.

“Taxes” means all taxes, including *ad valorem* taxes of the District, other than taxes imposed pursuant to Chapter 1 of Part 9 of the Law to secure general obligation bonds of the District or any improvement district thereof;

“Tender Agent” means the Bank of New York Mellon Trust Company, as Tender Agent under the Tender Agreement or any successor thereto.

“Tender Agreement” means the tender agent agreement dated as of June 1, 1996 by and between the District and the Tender Agent, as amended.

“Term” means the period commencing upon the effective date of the Installment Sale Agreement and ending upon the sooner to occur of (i) September 1, 2026; and (ii) the payment by the District of all amounts due under the Installment Sale Agreement; provided that notwithstanding the foregoing the Term shall not end prior to payment by District of all amounts due hereunder, including all amounts due to the Bank.

“Termination Date” means June 30, 2014, the stated expiration date of the Facility as such date may be extended, or any earlier date on which the Facility or Substitute Facility shall terminate, expire or be canceled.

“Trust Agreement” means the Trust Agreement by and among the District, the Corporation and the Trustee, dated as of July 1, 1996, as originally executed or as it may be amended from time to time as provided therein, including as amended by a First Supplement to Trust Agreement by and among the District, the Corporation and the Trustee, dated as of May 25, 2011.

“Water System” means all properties and assets, real and personal, tangible and intangible, of the District now or hereafter existing, used or pertaining to the production, treatment, transmission, distribution and sale of water, including all additions, extensions, expansions, improvements and betterments thereto, and equipments thereof; provided, however, that to the extent the District is not the sole owner of an asset or property, only the District’s ownership interest in such asset or property shall be considered a part of its Water System.

“Written Consent of the Corporation or District,” “Written Order of the Corporation or District,” “Written Request of the Corporation or District,” and “Written Requisition of the Corporation or District” mean, respectively, a written consent, order, request or requisition signed by or on behalf of (i) the Corporation by its President or a Vice President or (ii) the District by the Chairman of its Board of Directors or General Manager or by any person who is specifically authorized by resolution of the Board of Directors of the District to sign or execute such a document on its behalf.

## TRUST AGREEMENT

### CERTIFICATES; TERMS AND PROVISIONS

Transfer of Certificates. Any Certificate may, in accordance with its terms, be transferred upon the books required to be kept pursuant to the provisions of the Trust Agreement by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such Certificate for cancellation, accompanied by delivery of a written instrument of transfer in a form acceptable to the Trustee, duly executed. Transfer of any Certificate shall not be permitted by the Trustee (i) if the Trustee has received written notice from the Tender Agent during any Variable Rate Period that it has received notice from the Owner of such Certificate that such Certificate will be delivered to the Tender Agent for purchase on or before the next succeeding Interest Payment Date, (ii) during the fifteen (15) day period prior to the date designated by the Trustee for the selection of Certificates for prepayment, or (iii) if such Certificate has been called for prepayment or is then subject to mandatory tender pursuant to the Trust Agreement.

Whenever any Certificate shall be surrendered for transfer, the Trustee shall execute and shall deliver a new Certificate for a like aggregate principal amount of authorized denominations. The Trustee shall require the Certificate Owner requesting such transfer to pay any tax or other governmental charge required to be paid with respect to such transfer, and may in addition require the payment of a reasonable sum to cover expenses incurred by the District or the Trustee in connection with such transfer.

Exchange of any Certificate shall not be permitted by the Trustee (a) if the Trustee has received written notice from the Tender Agent during any Variable Rate Period that it has received notice from the Owner of such Certificate that such Certificate will be delivered to the Tender Agent for purchase on or before the next succeeding Interest Payment Date, (b) during the fifteen (15) day period prior to the date designated by the Trustee for the selection of Certificates for prepayment, or (c) if such Certificate has been called for prepayment or is then subject to mandatory tender pursuant to the Trust Agreement.

### VALIDITY OF CERTIFICATES

Validity of Certificates. The validity of the execution and delivery of the Certificates is not dependent on and shall not be affected in any way by any proceedings taken by the District, the Corporation or the Trustee with respect to or in connection with the Installment Sale Agreement. The recital contained in the Certificates that all acts, conditions and things required by the Constitution and statutes of the State of California and the Trust Agreement to exist, to have happened and to have been performed precedent to and in the delivery thereof do exist, have happened and have been performed in due time, form and manner as required by law shall be conclusive evidence of their validity and of compliance with the provisions of law in their delivery.

## INSTALLMENT PAYMENTS; FACILITY; SUBSTITUTE FACILITY

Deposit of Installment Payments. All Installment Payments to which the Corporation may at any time be entitled (including income or profit from investments), deposited by the District in the Installment Payment Fund pursuant to the Installment Sale Agreement, shall be paid directly to the Trustee pursuant to the terms of the Trust Agreement, and if received by the Corporation at any time shall be deposited by the Corporation with the Trustee within one Business Day after the receipt thereof, and the Trustee shall deposit all Installment Payments as and when received in the Certificate Payment Fund. All moneys at any time deposited in the Certificate Payment Fund shall be held by the Trustee in trust for the benefit of the Owners from time to time of the Certificates, and for the benefit of the Bank as provided in the Trust Agreement, but shall nevertheless be disbursed, allocated and applied solely for the uses and purposes set forth in the Trust Agreement.

Certificate Payment Fund. There is established with the Trustee the Certificate Payment Fund consisting of a District Payments Account and a Debt Service Account, which the Trustee covenants to maintain and hold in trust separate and apart from other funds held by it so long as any Installment Payments remain unpaid. The Trustee shall transfer from the Certificate Payment Fund the following amounts at the times and in the manner hereinafter provided, and shall deposit such amounts in one or more of the following respective accounts, each of which the Trustee shall establish and maintain and hold in trust separate and apart from other funds held by it, and each of which shall be disbursed and applied only as authorized in the Trust Agreement. Such amounts shall be so transferred to and deposited in the following respective Accounts:

1. All amounts paid by the District as Installment Payments shall be deposited in the District Payments Account. The Trustee shall also deposit to the Certificate Payment Fund all amounts required to be deposited thereunder in accordance with the Trust Agreement. The Trustee shall, in accordance with the Trust Agreement, make the necessary drawings under the Facility to pay the amounts specified in the Trust Agreement and deposit such amounts in the Debt Service Account. Subject to paragraph (b) below, the amounts on deposit in the Certificate Payment Fund shall be used solely for the payment of principal, mandatory prepayment, interest or the Purchase Price of the Certificates. After the Fixed Rate Conversion Date, on each date on which any payment of principal, mandatory prepayment, or interest is due with respect to the Certificates, the Trustee shall withdraw from the District Payments Account of the Certificate Payment Fund for application to payment of such debt service an amount equal to the debt service due on such Certificates on such date.

2. On each day on which the Trustee has received money drawn on the Facility in the amount specified in the Trust Agreement, the Trustee shall, not later than 4:00 p.m., New York City time, wire transfer to the Bank's account as specified in writing by the Bank from funds on deposit in the District Payments Account, if any, an amount equal to the amounts so drawn under the Facility. Notwithstanding anything to the contrary contained herein, in the event the Bank fails to honor a draw on the Facility in accordance with its terms, the Trustee shall pay the principal, prepayment price or interest due with respect to the Certificates from any Installment Payments on deposit in the District Payments Account regardless of whether such Installment Payments constitute Eligible Funds.

Surplus. Any surplus remaining in the Certificate Payment Fund, after prepayment and payment of all Certificates, including premiums (if any) and accrued interest, and payment of any applicable draws, accrued interest, fees and expenses to the Trustee and the Bank or provision for such prepayment and payment having been made to the satisfaction of the Trustee and the Bank, shall be withdrawn by the Trustee and remitted to the District.

Facility. The Trustee shall hold and maintain the Facility for the benefit of the Certificate Owners until the expiration date thereof. The Trustee shall diligently enforce all terms, covenants and conditions of the Facility, including payment when due of any use of the Facility, and will not consent to or agree to or permit any amendment or modification of the Facility which would materially adversely affect the rights or security of the Owners of the Certificates. If at any time during the term of the Facility, any successor Trustee shall be appointed and qualified under the Trust Agreement, the resigning or removed Trustee shall request that the Bank transfer the Facility to the successor Trustee. If the resigning or removed Trustee fails to make this request, the successor Trustee shall do so before accepting appointment. When any Facility expires in accordance with its terms or is replaced by a Substitute Facility, the Trustee shall immediately surrender such Facility to the issuing Bank.

In accordance with its terms, the Facility may be terminated as herein provided. The original Facility and any Substitute Facility shall be an obligation of the Bank to pay to the Trustee upon request made with respect to the Certificates related thereto and in accordance with the terms thereof:

(a) An amount, not exceeding the aggregate principal amounts of the Certificates, sufficient to pay the principal portion of the Purchase Price of the Certificates delivered or required to be delivered to the Tender Agent for purchase, or the principal amount of Certificates when due at their Stated Maturity or upon mandatory redemption or acceleration; and

(b) An amount, not exceeding interest on the Certificates for 34 days computed at the Maximum Rate, sufficient to pay the interest portion of the Purchase Price of Certificates delivered to the Tender Agent for purchase, or the interest accrued with respect to Certificates when due at their Stated Maturity or upon mandatory redemption, optional redemption or acceleration.

If a Facility is in effect with respect to the Certificates, the Trustee shall make a drawing under the Facility (in the manner and to the extent therein permitted) in an amount sufficient, and by the time required, to timely pay the principal of, interest on and the Purchase Price of the Certificates to become due at the Maturity thereof (upon their Stated Maturity, mandatory redemption, optional redemption or acceleration), or to timely pay the interest with respect to the Certificates to become due on each Interest Payment Date and Purchase Date, but in every case only in respect of Certificates which are not Bank Certificates, and the Trustee shall deposit the funds received from such a draw on the Facility in the Debt Service Account of the Certificate Payment Fund; provided, however, that, in the case of a prepayment of Certificates pursuant to the Trust Agreement, the Trustee shall not be required to present a draw under the Facility to the extent that the Trustee holds other Eligible Funds pursuant to the Trust Agreement in an amount sufficient to pay the Prepayment Price of the Certificates selected for prepayment on the prepayment date, and provided further that no draw shall be made under the Facility to pay the premium, if any, on the Certificates selected for prepayment. Without limiting the generality of the foregoing, at such time as the duration of the Rate Period is greater than one (1) month in duration, the Trustee is hereby instructed to draw upon the Facility on the first day of each calendar month during such Rate Period, commencing with the first day of the second month of such Rate Period (or on the Business Day preceding the first day of each such month, in the event such day is not a Business Day), an amount equal to the interest with respect to the Certificates that has accrued (or will accrue) during the month for which the drawing is being submitted, less, with respect to the final drawing of the Rate Period, investment earnings (if any) on any previous amounts drawn under the Facility, which investment earnings are on deposit in the Debt Service Account. All moneys held by the Trustee from draws on the Facility shall be held uninvested or, upon written direction of the District be, invested in non-callable, non-prepayable Federal Securities which mature not later than next Business Day. Notwithstanding the deposit of such moneys under the Trust Agreement and the subsequent reimbursement to the Bank, the District shall have no right, title or interest in such moneys and such moneys will be held exclusively for the Holders of the Certificates and paid over in accordance with the provisions of the Trust Agreement.

Payments of the principal of and interest with respect to Certificates representing interest at Variable Rates or CP Rates, whether at their Stated Maturity or upon their prepayment or acceleration, shall be made by the Trustee from the following sources in the order of priority indicated:

- (1) moneys paid to the Trustee from drawings under the Facility;
- (2) other Eligible Funds; and
- (3) any other moneys deposited by the District pursuant to the Installment Sale Agreement.

Upon and following the conversion of the Certificates to the Fixed Rate, the Certificates shall no longer be payable from or secured by the Facility or subject to tender for purchase.

Substitute Facility. If at any time the District shall deliver to the Trustee (1) a Substitute Facility, (2) an opinion of counsel stating that the delivery of such Substitute Facility to the Trustee is authorized under the Trust Agreement and complies with the terms hereof, (3) an Opinion of Bond Counsel that the proposed substitution will not adversely affect the exclusion of interest on the Certificates from gross income for federal income tax purposes, (4) one or more opinions of counsel addressed to the Trustee, to the effect, singly or together, that: (A) the Substitute Facility is a legal, valid and binding obligation of the obligor, enforceable against the obligor in accordance with its terms, except as limited by applicable reorganization, insolvency, liquidation, readjustment of debt, moratorium or other similar laws affecting the enforcement of the rights of creditors generally as such laws may be applied in the event of a reorganization, insolvency, liquidation, readjustment of debt or other similar proceeding of or moratorium applicable to the obligor and by general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law); and (B) payments made by the obligor under the Substitute Facility will not be voidable under Section 547 of the United States Bankruptcy Code in the context of a case or proceeding by or against the District or any Affiliates thereof under the United States Bankruptcy Code; (5) if a rating or ratings on the Certificates shall be in effect on the date of such substitution, written evidence from Moody's and/or Standard & Poor's, as applicable, to the effect that such rating agency has reviewed the proposed Substitute Facility and that the substitution of the proposed Substitute Facility for the existing Facility will not, by itself, result in a reduction or withdrawal of its rating on the Certificates, and (6) written evidence that notice of such proposed substitution has been sent to the Owners prior to such substitution, then the Trustee shall, so long as such Substitute Facility shall contain administrative procedures which are acceptable to the Trustee in its reasonable discretion, accept such Substitute Facility and promptly surrender the existing Facility to the issuer thereof.

Alternatively, if all of the requirements of the preceding paragraph are satisfied other than those set forth in clause (5) thereof, and the District has given the Trustee at least forty-five (45) days' written notice of its intention to substitute such Facility and simultaneously with such written notice the Trustee, the Remarketing Agent and the Tender Agent receive an Opinion of Bond Counsel to the effect that the substitution will not adversely affect the exclusion of the interest on the Certificates from gross income for federal income tax purposes, the Trustee shall accept the Substitute Facility, enforce payment of any amounts due under the existing Facility to the extent required by the Trust Agreement and thereupon surrender the existing Facility.

Any Substitute Facility shall be an irrevocable purchase agreement, letter of credit, surety bond, insurance policy, guaranty or other irrevocable credit facility, or any combination thereof, issued by one or more commercial banks or savings and loan associations, insurance companies or other financial institutions, the terms of which shall in all respects material to the interests of the Owners be the same as the Facility, except that the expiration date of such Substitute Facility may be later than the expiration date for the existing Facility and such expiration date shall be not less than one (1) year after the date such Substitute Facility is substituted for the existing Facility.

Investment of Moneys in Special Fund. Any moneys in the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account shall be invested by the Trustee upon the Written Request of the District, in Permitted Investments which will mature on or before the dates when such moneys are scheduled to be needed for payment from such fund and in accordance with the limitations set forth in the Trust Agreement, provided that moneys resulting from a draw on the Facility shall be invested solely in non-callable, non-prepayable Federal Securities maturing not later than the next business day or remain uninvested. Securities acquired as an investment of moneys in a fund shall be credited to such fund. Such Written Request of the District shall certify that the investment is a Permitted Investment.

In the absence of written investment direction from the District, the Trustee shall invest moneys held by it solely in Permitted Investments specified in clause (8) of the definition thereof unless otherwise directed in the Trust Agreement.

Such investments shall be valued by the Trustee as frequently as deemed necessary by the Bank, but not less often than semiannually, as set forth below, at the market value thereof, exclusive of accrued interest. Deficiencies in the amount on deposit in any fund or account resulting from a decline in market value shall be restored no later than the succeeding valuation date.

Any interest, profit or other income on such investments shall be deposited in the Certificate Payment Fund established under the Trust Agreement.

Subject to the further provisions of the Trust Agreement, the Trustee may sell or present for prepayment any obligations so purchased at the direction of the District whenever it shall be necessary in order to provide moneys to meet any payment, and the Trustee shall not be liable or responsible for any loss resulting from such investment. The Trustee and its affiliates may act as sponsor, advisor, depository, principal or agent in the acquisition or disposition of any investment and receive compensation in connection therewith. The Trustee may commingle any of the funds or accounts established pursuant to the Trust Agreement into a separate fund or funds for investment purposes only; provided, however, that all funds or accounts held by the Trustee hereunder shall be accounted for separately notwithstanding such commingling.

Pledge of Moneys in Funds. All amounts on deposit in the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account are irrevocably pledged to the Owners of the Certificates and the Bank as provided in the Trust Agreement. This pledge shall constitute a first and exclusive lien on the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account for the benefit of the Owners of the Certificates in accordance with the terms of the Trust Agreement and of the Installment Sale Agreement.

Corporation and District to Perform Installment Sale Agreement. The Corporation and District covenant and agree with the Owners of the Certificates to perform all obligations and duties imposed on them under the Installment Sale Agreement and, together with the Trustee, to enforce such Installment Sale Agreement against the other party thereto in accordance with its terms.

The Corporation and the District will in all respects promptly and faithfully keep, perform and comply with all the terms, provisions, covenants, conditions and agreements of the Installment Sale Agreement to be kept, performed and complied with by it.

The Corporation and the District agree not to do or permit anything to be done, or omit or refrain from doing anything, in any case where any such act done or permitted to be done, or any such omission of or refraining from action, would or might be a ground for cancellation or termination of the Installment Sale Agreement.

Tax Covenants. The Corporation and the District covenant with the Owners of the Certificates that, notwithstanding any other provision of the Trust Agreement, they will make no use of the proceeds of the Certificates that would cause the Certificates to be “arbitrage bonds” within the meaning of Section 148 of the Code.

The District will not make any use of the proceeds of the Certificates or any other funds of the District, or take or omit to take any other action, that would cause the Certificates to be “private activity bonds” within the meaning of Section 141 of the Code, or “federally guaranteed” within the meaning of Section 149(b) of the Code. To that end, so long as any Installment Payments are unpaid, the District, with respect to such proceeds and such other funds, will comply with all requirements of such Sections and all regulations of the United States Department of the Treasury issued thereunder and under Section 103 of the Internal Revenue Code of 1954, as amended, to the extent such requirements are, at the time, applicable and in effect.

The District will not use or permit the use of the Project or any portion thereof by any person other than a governmental unit as such term is used in Section 141 of the Code, in such manner or to such extent as would result in the loss of exclusion from gross income for federal income tax purposes of the portion of the Installment Payments constituting interest under Section 103 of the Code.

Accounting Records and Reports. The Trustee shall keep or cause to be kept proper books of record and account in which complete and correct entries shall be made of all transactions made by it relating to the receipts, disbursements, allocation and application of the Installment Payments, and such books shall be available for inspection by the District and by any Owner of Certificates, or his agent or representative, at reasonable hours and under reasonable conditions. Each month, so long as the Certificates are Outstanding, the Trustee shall furnish to the District a statement covering receipts, disbursements, allocation and application of amounts on deposit in the funds and accounts created hereunder held by it.

Compliance with Trust Agreement. The Trustee will not execute, or permit to be executed, any Certificates in any manner other than in accordance with the provisions of the Trust Agreement, and the District will not suffer or permit any default by it to occur under the Trust Agreement, but will faithfully observe and perform all the covenants, conditions and requirements hereof.

Observance of Laws and Regulations. To the extent necessary to assure their performance hereunder, the Corporation and the District will well and truly keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America, or of the State, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of any and every right, privilege or franchise now owned or hereafter acquired by the Corporation or the District, respectively, including its right to exist and carry on its business, to the end that such contracts, rights and franchises shall be maintained and preserved, and shall not become abandoned, forfeited or in any manner impaired.

Liens. So long as any Certificates are Outstanding, neither the District nor the Trustee, as assignee of the Corporation, will create or suffer to be created any pledge of or lien on the Installment Payments.

Prosecution and Defense of Suits. The Trustee, as assignee of the Corporation, to the extent indemnified by the District through the payment of Additional Costs under the Installment Sale Agreement, will defend against every action, suit or other proceeding at any time brought against the Trustee or any Owner upon any claim arising out of the receipt, deposit or disbursement of any of the Installment Payments or involving the rights of any Owner hereunder provided that the Trustee shall in no event be obligated to defend any such action, suit or proceeding if the District fails to indemnify the Trustee through the payment of Additional Costs under the Installment Sale Agreement or if such payment of Additional Costs is for any reason not made available to the Trustee; provided, further, that the Trustee

or any Owner at its or his election and at its or his sole cost and expense may appear in and defend any such action, suit or other proceeding.

Recordation and Filing. The District (pursuant to the Installment Sale Agreement) shall record, register, file, renew, refile and rerecord all such documents, including financing statements, as may be required by law in order to maintain a security interest in the Trust Agreement, the Installment Payments and Net Revenues, all in such manner, at such times and in such places as may be required by, and to the extent permitted by, law in order fully to preserve, protect and perfect the security of the Certificate Owners and the rights and security interests of the Trustee. The District shall (subject to the preceding paragraph) do whatever else may be necessary or be reasonably required in order to perfect and continue the lien of the Trust Agreement.

Further Assurances. Whenever and so often as requested so to do by the Trustee, Bank or any Certificate Owner, the Corporation and the District will promptly execute and deliver or cause to be executed and delivered all such other and further instruments, documents or assurances, and promptly do or cause to be done all such other and further things, as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Certificate Owners all rights, interest, powers, benefits, privileges and advantages conferred or intended to be conferred upon them by the Trust Agreement.

#### DEFAULT AND LIMITATION OF LIABILITY

Notice of Non-Payment. In the event of delinquency in the payment of any Installment Payments due by the District pursuant to the Installment Sale Agreement, the Trustee shall, after one Business Day following the date upon which such delinquent Installment Payment was due, immediately give written notice of the delinquency and the amount of the delinquency to the District, the Corporation and the Bank and notice of any other Event of Default within 30 days of knowledge thereof.

Action on Default or Termination. Upon the occurrence of an Event of Default, which shall also constitute a default under the Trust Agreement, and in each and every such case during the continuance of such Event of Default, the Trustee may exercise or shall if indemnified to its satisfaction exercise, as the case may be, any and all remedies available pursuant to law or granted pursuant to the Installment Sale Agreement. In determining whether a payment default has occurred or whether a payment on the Certificates has been made under the Trust Agreement, no effect shall be given to payments made under the Facility. The Trustee shall not take the Facility into account in determining whether the rights of Certificate holders are adversely affected by actions taken pursuant to the terms and provisions of the Trust Agreement or the Installment Sale Agreement; provided, however, that the Trustee shall not be able to require indemnification prior to an acceleration of the Certificates and the Installment Payments resulting from an Event of Default described in the Installment Sale Agreement the making a draw under the Facility or making a payment to the Holders of the Certificates.

The Bank shall be included as a party in interest and as a party entitled to (i) notify the Trustee of the occurrence of an Event of Default, and (ii) request the Trustee to intervene in judicial proceedings that affect the Certificates or the security therefor. The Trustee shall accept notice of default from the Bank.

Additionally, the Owners of Certificates, the Trustee on behalf of the Owners and the District shall have the right to bring suit, or exercise any other remedy available pursuant to law against the Bank to enforce any obligation of the Bank should it fail to perform any of its obligations under the Trust Agreement or under the Facility.

Anything in the Trust Agreement to the contrary notwithstanding, upon the occurrence and continuance of an Event of Default as defined therein, the Bank shall be entitled to control and direct the enforcement of all rights and remedies granted to the Certificate Owners or the Trustee for the benefit of the Certificate Owners under the Trust Agreement, including, without limitation: (i) the right to accelerate the principal of the Certificates (except with respect to an Event of Default which occurs as the result of the

receipt by the Trustee of written notice from the Bank that it has not reinstated the interest component of the Facility) as described in the Trust Agreement, and (ii) the right to annul any declaration of acceleration, and the Bank shall also be entitled to approve all waivers of Events of Default.

Upon the occurrence of an Event of Default, the Trustee may, with the consent of the Bank, and shall, at the direction of the Bank or 50% of the Certificate Owners with the consent of the Bank, by written notice to the District and the Bank, declare the principal of the Certificates to be immediately due and payable, whereupon that portion of the principal of the Certificates thereby coming due and the interest thereon accrued to the date of payment shall, without further action, become and be immediately due and payable, anything in the Trust Agreement or in the Certificates to the contrary notwithstanding.

Upon declaration of the entire principal amount of the unpaid Installment Payments and the accrued interest thereon to be due and payable immediately and provided such declaration is not rescinded or annulled, all in accordance with the Installment Sale Agreement, the Trustee may apply all moneys received as Installment Payments and all moneys held in any fund or account hereunder (other than the Rebate Fund) in the manner provided in the Trust Agreement. Upon declaration of an acceleration, interest on the Certificates shall cease to accrue.

Application of Moneys Collected by Trustee. Any moneys collected (excluding moneys drawn under the Facility) by the Trustee pursuant to the Trust Agreement after an Event of Default has occurred shall be applied in the order following, at the date or dates fixed by the Trustee and, in the case of distribution of such moneys on account of principal (or premium, if any) or interest, upon presentation of the Certificates, and stamping thereon the payment, if only partially paid, and upon surrender thereof, if fully paid:

First: To the payment of all costs and expenses of collection, just and reasonable compensation to the Trustee for its own services and for the services of counsel, agents and employees by it properly engaged and employed, and all other expenses and liabilities incurred, pursuant to the provisions of the Trust Agreement, together with interest on all such amounts advanced by the Trustee at the highest rate permitted by law.

Second: In case the principal of none of the Certificates shall have become due and remains unpaid, to the payment of interest in default, such payments to be made ratably and proportionately to the persons entitled thereto.

Third: In case the principal of the Certificates shall have become due by acceleration or otherwise and remains unpaid, first to the payment of interest in default and then to the payment of principal of the Certificates then due and unpaid, in every instance such payment to be made ratably to the persons entitled thereto.

Fourth: Additional Costs.

If such moneys are invested, they shall be invested only in Permitted Investments having a maturity of thirty (30) days or less.

Other Remedies of the Trustee. The Trustee, with the consent of the Bank, and upon being indemnified to its satisfaction therefor, in its discretion may:

I. by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the District or any director, officer or employee thereof, and to compel the District or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Trust Agreement;

2. by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

3. by suit in equity upon the happening of any default hereunder to require the District and its directors, officers and employees to account as the trustee of an express trust.

Trustee to Represent Owners. The Trustee is irrevocably appointed (and the successive respective Owners of the Certificates by taking and holding the same, shall be conclusively deemed to have so appointed the Trustee) as trustee and true and lawful attorney in fact of the Owners of the Certificates for the purpose of exercising and prosecuting on their behalf such rights and remedies as may be available to such Owners under the provisions of the Certificates, the Trust Agreement, the Installment Sale Agreement and applicable provisions of law. Upon the occurrence and continuance of an event of default or other occasion giving rise to a right in the Trustee to represent the Owners, the Trustee in its discretion may, and upon the written request of the Owners of not less than twenty-five percent (25%) in aggregate principal amount of the Certificates then Outstanding, and upon being indemnified to its satisfaction therefor, shall, proceed to protect or enforce its rights or the rights of such Owners by such appropriate action, suit, mandamus or other proceedings as it shall deem most effectual to protect and enforce any such right, at law or in equity, either for the specific performance of any covenant or agreement contained herein, or in aid of the execution of any power herein granted, or for the enforcement of any other appropriate legal or equitable right or remedy vested in the Trustee or in such Owners under the Trust Agreement, the Installment Sale Agreement or any law; and upon instituting such proceeding, the Trustee shall be entitled, as a matter of right, to the appointment of a receiver of the Net Revenues and other assets pledged under the Trust Agreement pending such proceedings. All rights of action under the Trust Agreement or the Certificates or otherwise may be prosecuted and enforced by the Trustee without the possession of any of the Certificates or the production thereof in any proceeding relating thereto, and any such suit, action or proceeding instituted by the Trustee shall be brought in the name of the Trustee for the benefit and protection of all the Owners of such Certificates, subject to the provisions of the Trust Agreement.

Owners' Direction of Proceedings. Subject to the rights of the Bank to control proceeding in the Trust Agreement, the Owners of a majority in aggregate principal amount of the Certificates then Outstanding shall have the right, by an instrument or concurrent instruments in writing executed and delivered to the Trustee, together with indemnity satisfactory to the Trustee, to direct the method of conducting all remedial proceedings taken by the Trustee under the Trust Agreement, provided that such direction shall not be otherwise than in accordance with law and the provisions of the Trust Agreement, and that the Trustee shall have the right to decline to follow any such direction which in the opinion of the Trustee would be unjustly prejudicial to Owners of Certificates not parties to such direction or may result in individual liability for the Trustee. The Trustee shall not be liable for any actions performed at the direction of the Owners of the Certificates given pursuant to the Trust Agreement.

No Owner of any Certificate shall have the right to institute any such action or proceeding at law or in equity, for the protection or enforcement of any right or remedy under the Trust Agreement, the Installment Sale Agreement or any applicable law with respect to such Certificate, unless (1) such Owner shall have given to the Trustee written notice of the occurrence of an Event of Default; (2) the Owners of not less than 25% in aggregate principal amount of the Certificates then Outstanding shall have made written request upon the Trustee to exercise the powers granted or to institute such suit, action or proceeding in its own name; (3) such Owner or said Owners shall have tendered to the Trustee reasonable indemnity against the costs, expenses and liabilities to be incurred in compliance with such request; and (4) the Trustee shall have refused or omitted to comply with such request for a period of sixty (60) days after such written request shall have been received by, and said tender of indemnity shall have been made to, the Trustee.

Such notification, request, tender of indemnity and refusal or omission are hereby declared, in every case, to be conditions precedent to the exercise by any Owner of Certificates of any remedy under the Trust Agreement or under law; it being understood and intended that no one or more Owners of Certificates shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Trust Agreement or the rights of any other Owners of Certificates, or to enforce any right under the Trust Agreement, the Installment Sale Agreement or other applicable law with respect to the Certificates, except in the manner therein provided, and that all proceedings at law or in equity to enforce any such right shall be instituted, had and maintained in the manner herein provided and for the benefit and protection of all Owners of the Outstanding Certificates, subject to the provisions of the Trust Agreement.

Notwithstanding any other provision in the Trust Agreement, each Owner shall have the right to receive payment of the principal and the premium, if any, and interest represented by its Certificate at the respective dates on which the same became due and payable in accordance with the terms, from the source and in the manner provided in such Certificate and in the Trust Agreement, and to institute suit for the enforcement of any such payment, and such rights shall not be impaired without the consent of such Owner.

Non-Waiver. A waiver of any default or breach of duty or contract by the Trustee shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee or the Owners of the Certificates to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or an acquiescence therein, and every right or remedy conferred upon the Trustee by law or by this article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee or the Owners of the Certificates, the Trustee, the Owners of the Certificates and the District shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Trust Agreement conferred upon or reserved to the Trustee or the Owners of the Certificates is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given under the Trust Agreement or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by any law.

No Obligation of the District to the Owners. Except for the payment of Installment Payments when due in accordance with the Installment Sale Agreement and the performance of the other covenants and agreements of the District contained in said Installment Sale Agreement and in the Trust Agreement, the District shall have no obligation or liability to the Owners of the Certificates with respect to the Trust Agreement or the execution, delivery or transfer of the Certificates, or the disbursement of Installment Payments to the Owners by the Trustee; provided however that nothing contained in this paragraph shall affect the rights, duties or obligations of the Trustee expressly set forth in the Trust Agreement.

No Obligation with Respect to Performance by Trustee. Neither the District nor the Corporation shall have any obligation or liability to any of the other parties to the Trust Agreement or to the Owners of the Certificates with respect to the performance by the Trustee of any duty imposed upon it under the Trust Agreement.

No Liability to Owners for Payment. The Corporation shall not have any obligation or liability to the Owners of the Certificates with respect to the payment of the Installment Payments by the District when due, or with respect to the performance by the District of any other covenant made by it in the Installment Sale Agreement or in the Trust Agreement. Except as provided in the Trust Agreement, the Trustee shall not have any obligation or liability to the Owners of the Certificates with respect to the payment of the Installment Payments by the District when due, or with respect to the performance by the District of any other covenant made by it in the Installment Sale Agreement or in the Trust Agreement.

No Responsibility for Sufficiency. The Trustee shall not be responsible for the sufficiency of the Trust Agreement, the Installment Sale Agreement, or of the assignment made to it under the Trust Agreement of rights to receive Installment Payments pursuant to the Installment Sale Agreement, or the value of or title to the Project. The Trustee shall not be responsible or liable for any loss suffered in connection with any investment of funds made by it under the terms of and in accordance with the Trust Agreement.

#### AMENDMENT OF TRUST AGREEMENT

Amendments Permitted. The Trust Agreement and the rights and obligations of the District and of the Owners of the Certificates and of the Trustee may be modified or amended at any time by an amendment thereto which shall become binding when the written consents of the Bank and the Owners of a majority in aggregate principal amount of the Certificates then Outstanding, exclusive of Certificates disqualified as provided in the Trust Agreement, shall have been filed with the Trustee and the Bank. No such modification or amendment shall (1) extend the stated maturities of the Certificates, or reduce the rate of interest represented thereby, or extend the time of payment of interest, or reduce the amount of principal represented thereby, or reduce any premium payable on the prepayment thereof, or impair the right of any Owner to tender such Owner's Certificate as provided for in the Trust Agreement, without the consent of the Owner of each Certificate so affected, or (2) reduce the aforesaid percentage of Owners of Certificates whose consent is required for the execution of any amendment or modification of the Trust Agreement, or (3) modify any of the rights or obligations of the Trustee, the Bank or the District without its written consent thereto.

The Trust Agreement and the rights and obligations of the Corporation, the Trustee, the District and of the Owners of the Certificates may also be modified or amended at any time by an amendment thereto which shall become binding upon execution and receipt of the written consent of the Bank but without the consent of the Owners of any Certificates, but only to the extent permitted by law and only for anyone or more of the following purposes:

- (1) to add to the covenants and agreements of the Corporation or the District contained in the Trust Agreement other covenants and agreements thereafter to be observed or to surrender any right or power herein reserved to or conferred upon the Corporation or the District, and which shall not adversely affect the interests of the Owners of the Certificates;
- (2) to cure, correct or supplement any ambiguous or defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement, as the Corporation or the District may deem necessary or desirable and which shall not adversely affect the interests of the Owners of the Certificates;
- (3) to provide, if necessary, for more than one financial institution or insurance company to be the issuer of the Facility as permitted in the Trust Agreement; and
- (4) to make such other amendments or modifications as may be necessary in order to obtain a rating on the Certificates from Standard & Poor's Corporation, Moody's Investors Service or any other nationally recognized rating services or which otherwise may be in the best interests of the Owners of the Certificates.

The Trustee shall have received an opinion of Special Counsel to the effect that such amendment or modification will not adversely affect the exclusion from gross income, for purposes of Section 103 of the Code, of interest on the Certificates.

Endorsement or Replacement of Certificates After Amendment or Supplement. After the effective date of any action taken as provided in the Trust Agreement, the Trustee may determine that the Certificates may bear a notation by endorsement in form approved by the Trustee as to such action, and in that case upon demand of the Trustee to the Owner of any Outstanding Certificate and presentation of such Owner's Certificate for such purpose at the principal corporate trust office of the Trustee a suitable notation as to such action shall be made on such Certificate. If the Trustee shall so determine, new Certificates so modified as in the opinion of the Trustee shall be necessary to conform to such action shall be prepared, and in that case upon demand of the Trustee to the Owner of any Outstanding Certificates such new Certificates shall be exchanged at the principal corporate trust office of the Trustee without cost to each Owner for Certificates then Outstanding upon surrender of such Outstanding Certificates.

Amendment of Particular Certificates. The provisions of the Trust Agreement will not prevent any Owner from accepting any amendments to the particular Certificates held by him, provided that due notation thereof is made on such Certificates.

#### DEFEASANCE

Discharge of Trust Agreement. When the obligations of the District under the Installment Sale Agreement shall cease pursuant to the Installment Sale Agreement (except for the right of the Trustee and the obligation of the District to have the Eligible Funds and Permitted Investments mentioned therein applied to the payment of Installment Payments as therein set forth and the obligation to apply moneys on deposit in the Rebate Fund), then in that case the obligations created by the Trust Agreement shall thereupon cease, terminate and become void except for the obligation of the District to direct the Trustee to apply money on deposit in the Rebate Fund as provided in the Trust Agreement which shall continue until such moneys are so applied and the right of the Owners to have applied and the obligation of the Trustee to apply such Eligible Funds and Permitted Investments to the payment of the Certificates as set forth in the Trust Agreement and, subject to application of moneys on deposit in the Rebate Fund, the Trustee shall turn over to the District, after provision for payment of amounts due the Trustee thereunder, as an overpayment of Installment Payments, any surplus in the Certificate Payment Fund and all balances remaining in any other funds or accounts other than moneys and Permitted Investments held for the payment of the Certificates at maturity or on prepayment, which moneys and Permitted Investments shall continue to be held by the Trustee in trust for the benefit of the Owners and shall be applied by the Trustee to the payment, when due, of the principal and interest and premium, if any, represented by the Certificates, and after such payment, the Trust Agreement shall become void.

Deposit of Money or Securities with Trustee. During the Fixed Rate Period and whenever in the Trust Agreement or the Installment Sale Agreement it is provided or permitted that there be deposited with or held in trust by the Trustee Eligible Funds or securities acquired with Eligible Funds in the necessary amount to pay or prepay any Certificates, the Eligible Funds or securities to be so deposited or held may include Eligible Funds or securities held by the Trustee in the funds and accounts established pursuant to the Trust Agreement and shall be:

1. lawful money of the United States of America in an amount equal to the principal amount represented by such Certificates and all unpaid interest represented thereby to maturity, except that, in the case of Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment shall have been given or provision satisfactory to the Trustee shall have been made for the giving of such notice, the amount to be deposited or held shall be the principal amount or Prepayment Price and all unpaid interest to such date of prepayment if any, represented by such Certificates; or

2. non-callable, non-prepayable Federal Securities described in clause (a) of the definition thereof which will provide money sufficient to pay the principal at maturity or upon prepayment plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment shall have been given or provision satisfactory to the Trustee shall have been made for the giving of such notice;

together with a certificate of an Independent Certified Public Accountant that such amount on deposit, together with interest to accrue thereon and moneys on deposit in the funds and accounts provided for in the Trust Agreement, will be fully sufficient to pay and discharge the obligation to pay the Certificates (including all principal, interest and prepayment premiums) at or before their respective maturity dates, together with an Opinion of Bond Counsel that such deposit will not adversely affect the tax-exempt status of interest on the Certificates; provided, in each case, that the Trustee shall have been irrevocably instructed (by the terms of the Trust Agreement and the Installment Sale Agreement or by Written Request of the District) to apply such money or securities to the payment of such principal or Prepayment Price and interest represented by such Certificates.

Whenever moneys have been deposited with the Trustee pursuant to the Trust Agreement which are insufficient to pay all Outstanding Certificates, the Trustee, at the direction of the District, shall identify the Certificates to be deemed defeased and prepaid at the next Prepayment Date.

Notwithstanding anything in the Trust Agreement to the contrary, in the event that the principal coming due on the Certificates shall be paid by the Bank pursuant to the Facility, the Certificates shall remain Outstanding for all purposes, not be defeased or otherwise satisfied and not be considered paid by the District, and the assignment and pledge of the trust created hereunder and all covenants, agreements and other obligations of the District to the Registered Owners of the Certificates shall continue to exist and shall run to the benefit of the Bank, and the Bank shall be subrogated to the rights of such Registered Owners of the Certificates.

Unclaimed Moneys. Anything contained in the Trust Agreement to the contrary notwithstanding, any moneys held by the Trustee in trust for the payment and discharge of the interest or principal or Prepayment Price represented by any of the Certificates which remain unclaimed for two years after the date of deposit of such moneys if deposited with the Trustee after the date when the interest and principal or Prepayment Price represented by such Certificates have become payable, shall at the Written Request of the District be repaid by the Trustee to the District as its absolute property free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the District for the payment of the interest and principal or Prepayment Price represented by such Certificates; provided, however, that before being required to make any such payment to the District, the Trustee shall first mail a notice to the Owners of the Certificates so payable, at the address of such Owners as shown on the certificate registration books maintained by the Trustee, that such moneys remain unclaimed and that after a date named in such notice, which date shall not be less than thirty (30) days after the date of the mailing of such notice, the balance of such moneys then unclaimed will be returned to the District.

#### MISCELLANEOUS

Benefits of Trust Agreement Limited to Parties. Nothing in the Trust Agreement expressed or implied is intended or shall be construed to confer upon, or to give or grant to, any person or entity, other than the District, the Trustee, the Bank and the Registered Owners of the Certificates, any right, remedy or claim under or by reason of the Trust Agreement or any covenant, condition or stipulation hereof, and all covenants, stipulations, promises and agreements in the Trust Agreement contained by and on behalf of the District shall be for the sole and exclusive benefit of the District, the Trustee, the Bank and the Registered Owners of the Certificates.

Disqualified Certificates. Certificates owned or held by or for the account to the Corporation or the District (but excluding Certificates held in any pension or retirement fund) shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding Certificates provided for in the Trust Agreement, and shall not be entitled to consent to or take any other action provided for in the Trust Agreement.

The Trustee may adopt appropriate regulations to require each Owner of Certificates, before his consent provided for in the Trust Agreement shall be deemed effective, to reveal if the Certificates as to which such consent is given are disqualified as provided in the Trust Agreement.

Waiver of Personal Liability. No director, officer or employee of the District or the Corporation shall be individually or personally liable for the payment of the interest or principal or the prepayment premiums, if any, represented by the Certificates, but nothing contained in the Trust Agreement shall relieve any director, officer or employee of the District or Corporation from the performance of any official duty provided by any applicable provisions of law or by the Installment Sale Agreement or the Trust Agreement.

California Law. The Trust Agreement will be construed and governed in accordance with the laws of the State of California.

## **INSTALLMENT SALE AGREEMENT**

### **ACQUISITION AND CONSTRUCTION OF THE PROJECT; ADDITIONAL COSTS**

Changes to the Project. The District may substitute other improvements for those listed as components of the Project in the Installment Sale Agreement, but only if the District first files with the Corporation and the Trustee a statement of the District:

- (a) identifying the improvements to be substituted and the improvements to the District's facilities they replace in the Project; and
- (b) stating that the estimated costs of construction, acquisition and installation of the substituted improvements are not less than such costs for the improvements previously planned; together with an Opinion of Bond Counsel.

Title. All right, title and interest in each component of the Project (as described in the Installment Sale Agreement) will automatically vest in the District upon completion of such component. Such automatic vesting shall occur without further action by the Corporation, and the Corporation shall, if requested by the District or if necessary to assure such automatic vesting of such interests of title, deliver any and all documents required to assure such vesting.

Additional Costs. After making the Installment Payments, the District shall pay additional costs hereunder ("Additional Costs") any amounts required to be rebated to the United States pursuant to Section 148(f) of the Code in order to maintain the exclusion from gross income of interest represented by the Certificates for purposes of federal income taxation, all costs incurred in connection with the Facility, all amounts due with respect to Bank Certificates, including principal and all accrued and unpaid interest at the Bank Rate, and such amounts in each year as shall be required for the payment of all costs and expenses incurred in connection with the sale to District of the Project, including payment of any fees, costs and expenses in connection with the administration of the Project, payment of all taxes, assessments and governmental charges of any nature whatsoever hereafter levied or imposed by any governmental authority against the Corporation or the Installment Payments and other payments referred to herein, to be made by District (except for income taxes of the Corporation), and payment of all fees, costs and expenses incurred by the Corporation with the prior approval of the District.

## COVENANTS OF DISTRICT

Compliance with Installment Sale Agreement and Ancillary Agreements. The District will punctually pay the Installment Payments and Additional Costs in strict conformity with the terms of the Installment Sale Agreement, and will faithfully observe and perform all the agreements, conditions, covenants and terms contained therein required to be observed and performed by it, and will not terminate the Installment Sale Agreement for any cause including, without limiting the generality of the foregoing, any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Project, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State of California or any political subdivision of either or any failure of the Corporation to observe or perform any agreement, condition, covenant or term contained herein required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected herewith or the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Corporation or any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lock outs, lack of transportation facilities, fire, explosion, or acts or regulations of governmental authorities.

The District will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Trust Agreement required to be observed and performed by it, and it is expressly understood and agreed by and among the parties to the Installment Sale Agreement and the Trust Agreement that each of the agreements, conditions, covenants and terms contained in each such agreement is an essential and material term of the purchase of and payment for the Project by the District pursuant to, and in accordance with, and as authorized under the Law.

Annual Budget. During the Term of the Installment Sale Agreement, the District agrees and covenants to take such action as may be necessary to include all Installment Payments and Additional Costs due under the Installment Sale Agreement in its annual budget and to make the necessary annual appropriations for all such Installment Payments and Additional Costs.

Tax Covenants. The District covenants that, notwithstanding any other provision of the Installment Purchase Agreement, it will make no use of the proceeds of the Certificates or of any other amounts, regardless of the source, or of any property or take no action, or refrain from taking any action, that would cause the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The District will not use or permit the use of the Project or any portion thereof by any person other than a governmental unit as such term is used in Section 141 of the Code, in such manner or to such extent as would result in the loss of exclusion from gross income for federal income tax purposes of the portion of the Installment Payments constituting interest under Section 103 of the Code. The District will not make any use of the proceeds of the Certificates or any other funds of the District, or take or omit to take any other action, that would cause the obligation provided herein to be "federally guaranteed" within the meaning of Section 149(b) of the Code or "private activity bonds" within the meaning of Section 141 of the Code. To that end, so long as any Installment Payments and Additional Costs are unpaid, the District, with respect to such proceeds and such other funds, will comply with all requirements of such Sections and all regulations of the United States Department of the Treasury issued thereunder and under Section 103 of the Internal Revenue Code of 1954, as amended, to the extent such requirements are, at the time, applicable and in effect.

Collection of Rates and Charges. The District will fix, prescribe and collect rates, fees and charges for the services and commodities provided by the Water System which will be sufficient to yield (i) Taxes and Net Revenues during each Fiscal Year in an amount not less than 120% of the sum of the Installment Payments provided for under the Installment Sale Agreement and on any Parity Debt for such Fiscal Year. On or before the first day of the eighth month of each Fiscal Year, the District will complete a review of its financial condition for the purpose of estimating whether the Taxes and Net Revenues for the then current Fiscal Year will be sufficient to meet the requirements of this section, which review shall be evidenced by a certificate of an Authorized Officer of the District that shall be filed with the Trustee within ten (10) days of

the completion of such review. If such certificate shows that such Taxes and Net Revenues may not be sufficient to meet the requirements of this section, the District will promptly take such action as shall be necessary and sufficient to comply with these requirements, and will promptly advise the Trustee as to such action taken. The District may make adjustments from time to time in such rates, fees and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates, fees and charges then in effect unless the Net Revenues from such reduced rates, fees and charges will at all times be sufficient to meet the requirements of this paragraph.

Rules and Regulations. To the extent permitted by law, the District shall have in effect at all times rules and regulations requiring each consumer or customer located within the service area of the Water System to pay the tolls, rates, fees and charges applicable to the service and commodities provided by the Water System to such premises and providing for the billing thereof and for a due date and a delinquency date for each bill. The District will not permit any part of the Water System, or any facility thereof, to be used or taken advantage of free of charge by any person, firm or corporation, or by any public agency (including the United States of America, the State of California and any public corporation, political subdivision, city, county, district or agency of any thereof); provided, however, that the District may without charge use the services and commodities provided by the Water System. Nothing contained in this paragraph shall prohibit incidental use of Water System facilities by any person, firm, corporation or public agency where such use does not in any manner impair or adversely affect the rights or security of the Certificate Owners.

Insurance. The District shall at all times keep or cause to be kept the properties of the Water System which are of an insurable nature and of the character usually insured by those operating properties similar to the Water System insured against loss or damage by fire and from other causes customarily insured against and in such relative amounts as are usually obtained so long as such insurance is obtainable at reasonable costs. To the extent obtainable at reasonable cost, the District shall at all times use its reasonable efforts to maintain or cause to be maintained insurance or reserves against loss or damage from such hazards and risks to the person and property of others as are usually insured or reserved against by those operating properties similar to the properties of the Water System. To the extent obtainable at reasonable cost, the District shall also use its reasonable efforts to maintain or cause to be maintained any additional or other insurance which it shall deem necessary or advisable to protect its interests and those of the Certificate Owners. Any such insurance shall be in the form of policies or contracts for insurance with insurers of good standing and shall include a loss payable clause making any loss thereunder payable to the Trustee as its interests appear. The District will procure and maintain with responsible insurers workers' compensation insurance against liability for compensation under the Workers Compensation Insurance and Safety Act of California or any act amendatory thereof or supplemental thereto, which insurance shall cover all persons employed in connection with the Water System; provided that such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and manner usually maintained in connection with systems similar to the Water System. Anything in the Installment Sale Agreement to the contrary notwithstanding, the District may be self-insured for all or any part of the foregoing requirements.

Net Proceeds of Insurance. All proceeds of insurance against property damage and all proceeds of condemnation awards relating to the Project shall be payable to the District alone, and the District shall retain and collect such proceeds. All claims under any such insurance policy or with respect to any condemnation proceeding relating to the Project may be settled by the District without the consent of the Corporation or the Trustee. Such proceeds shall be applied promptly to the optional prepayment of Installment Payments, or retained by the District and promptly applied to the repair or rebuilding of the Project or the acquisition or construction of the capital improvements to the Water System.

Payment of Taxes and Assessments; Compliance With Law. The District will from time to time duly pay and discharge, or cause to be paid and discharged, all taxes, assessments and other governmental charges, or required payments in lieu thereof, lawfully imposed upon the properties of the District or upon the rights, revenues, income, receipts, and other moneys, securities and funds of the District, when the same

shall become due (including all rights, moneys and other property transferred, assigned or pledged under the Installment Sale Agreement), and all lawful claims for labor and material and supplies, except those taxes, assessments, charges or claims which the District shall in good faith contest by proper legal proceedings if the District shall in all such cases have set aside on its books reserves deemed adequate with respect thereto. Nothing contained in the Installment Sale Agreement shall require the District to pay any taxes, assessments and other governmental charges which have accrued but are not yet payable, nor shall anything in the Installment Sale Agreement require the District to satisfy any claim or lien for labor, materials or supplies in connection with work performed by for which payment is not yet due.

Financing Statements. The District shall promptly file in accordance with the applicable provisions of the Act and the Uniform Commercial Code in effect in the State of California, all financing statements or similar notices required to fully perfect and continue the perfection of the security interest granted under the Installment Sale Agreement in (i) the proceeds of the sale of the Certificates, (ii) the Taxes and Net Revenue, and (iii) all Funds and Accounts pledged by the Trust Agreement including the investments, if any, thereof. On or before February 1 of each year, the District shall deliver to the Trustee a certificate of an authorized officer of the District to the effect that all filings and other actions then required to continue the perfection of the security interest granted under the Installment Sale Agreement or under the Trust Agreement have been accomplished and setting forth all such filings made and actions taken since the previous such certificate was delivered to the Trustee.

Corporate Existence. The District shall at all times maintain its corporate existence and shall do and perform or cause to be done and performed all acts and things required to be done or performed by or on behalf of the District under the Installment Sale Agreement and the provisions of the Trust Agreement.

Senior Debt. The District shall not incur any obligation payable from the Net Revenues senior to the obligation to make the Installment Payments and shall not sell any portion of the Water System which would impair the ability of the District to make Installment Payments, except that the District may acquire and sell portions of the Water System in the ordinary course of business.

#### PREPAYMENT OF INSTALLMENT PAYMENTS AND DISCHARGE OF OBLIGATIONS

Prepayment. The District shall have the right at any time or from time to time to prepay all or any part of the Installment Payments to the extent that Certificates may be prepaid in accordance with the Trust Agreement, by paying the applicable prepayment price together with accrued interest to the date of prepayment and the Corporation agrees that the Trustee shall accept such prepayments when the same are tendered by the District. Prepayments may be made by payments of Eligible Funds or surrender of Certificates, as contemplated by the Installment Sale Agreement. All such prepayments (and the additional payment of any amount necessary to pay the applicable premiums, if any, payable in Eligible Funds upon the prepayment of Certificates) shall be deposited upon receipt in the Prepayment Account and, at the Request of the District, credited against Installment Payments in order of their due date or used for the prepayment or purchase of Outstanding Certificates in the manner and subject to the terms and conditions set forth in the Trust Agreement. The District shall also have the right to surrender Certificates acquired by it in any manner whatsoever to the Trustee for cancellation, and such Certificates, upon such surrender and cancellation, shall be deemed to be paid and retired, and shall be allocated as set forth in the Trust Agreement. Notwithstanding any such prepayment or surrender of Certificates, as long as any Certificates remain Outstanding, or any Installment Payments or Additional Costs remain unpaid, the District shall not be relieved of its obligations hereunder.

If the District is not in default in the payment of any Additional Costs, the Trustee, at the request of the District, at any time that there is on deposit with the Trustee Eligible Funds or securities acquired with Eligible Funds in the amount necessary to pay or redeem all Certificates Outstanding (as provided in the Trust Agreement), shall forthwith take all steps necessary to discharge and defease the entire indebtedness on all Certificates Outstanding and all covenants, agreements and other obligations of the Corporation or District under the Trust Agreement.

The District also may prepay all or any part of its obligations hereunder and prepay the Certificates pursuant to the Trust Agreement by depositing with the Trustee in the Prepayment Fund Net Proceeds from hazard insurance or condemnation proceeds received with respect to the Water System.

Discharge of Obligations. When:

(a) all Installment Payments shall have become due and payable in accordance with the Installment Sale Agreement or a written notice of the District to prepay all of the Installment Payments shall have been filed with the Corporation; and

(b) during any period the Certificates represent interest calculated at a Fixed Rate there shall have been deposited with the Trustee at or prior to the Installment Payment Dates or date (or dates) specified for prepayment, in trust for the benefit of the Corporation or its assigns and irrevocably appropriated and set aside to the payment of the Installment Payments, sufficient Eligible Funds and/or non-callable, non-prepayable Federal Securities described in clause (a) of the definition thereof acquired with Eligible Funds, the principal of and interest on which when due will provide money sufficient to pay all principal, prepayment premium, if any, and interest of the Installment Payments to their respective Payment Dates or prepayment date or dates as the case may be; and

(c) none of the Installment Payments shall remain unpaid, and provision shall have been made for the payment of all other Additional Costs (including all fees and expenses of the Trustee and the Bank),

then and in that event, the right, title and interest of the Corporation therein and the obligations of the District under the Installment Sale Agreement shall thereupon cease, terminate, become void and be completely discharged and satisfied (except for the right of the Trustee and the obligation of the District to have such moneys and such Federal Securities applied to the payment of the Installment Payments and the covenants of the District as set forth in the Installment Sale Agreement, which shall survive the discharge of the Installment Sale Agreement). In such event, upon request of the District, the Trustee shall cause an accounting for such period or periods as may be requested by the District to be prepared and filed with the District and shall execute and deliver to the District all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee shall pay over to the District, as an overpayment of Installment Payments, all such moneys or such Federal Securities held by it pursuant to the Installment Sale Agreement or pursuant to the Trust Agreement other than such moneys and such Federal Securities as are required for the payment or prepayment of the Installment Payments, which moneys and Federal Securities shall continue to be held by the Trustee in trust for the payment of the Installment Payments and shall be applied by the Trustee to the payment of the Installment Payments of the District.

#### EVENTS OF DEFAULT AND REMEDIES

Events of Default Defined. The following shall be “events of default” under the Installment Sale Agreement and the terms “event of default” and “default” shall mean, whenever they are used in the Installment Sale Agreement, anyone or more of the following events:

(a) Failure by the District to pay any Installment Payment required to be paid under the Installment Sale Agreement at the time set forth therein;

(b) Failure by the District to observe and perform any covenant, condition or agreement on its part to be observed or performed, other than as referred to in the foregoing paragraph (a) for a period of 30 days after written notice by the Corporation, the Trustee, the Bank, if the Facility shall then be in effect, or the Owners of not less than twenty-five percent (25%) in aggregate principal amount of Certificates then Outstanding to the District specifying such failure and requesting that it be remedied; provided, however, if the failure stated in the notice cannot be

corrected within the applicable period, the Corporation, the Trustee, the Bank and such Owners will not unreasonably withhold consent to an extension of such time if corrective action is instituted by the District within the applicable period and diligently pursued until the default is corrected;

(c) Inability of the District to generally pay its debts as such debts become due, or admission by the District, in writing, of its inability to pay its debts generally, or the making by the District of a general assignment for the benefit of creditors, or the institution of any proceeding by or against the District seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding-up, reorganization, reimbursement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or for appointment of a receiver, trustee, or other similar officer of it or any substantial part of its property, or the taking of any action by the District to authorize any of the actions set forth above in this paragraph; and

(d) Any event of default with respect to Parity Debt; and

(e) Receipt by the Trustee of written notice from the Bank of the occurrence of an event of default under the Reimbursement Agreement and electing to exercise remedies available to it under the Reimbursement Agreement, the Trust Agreement and under the Installment Sale Agreement.

Notwithstanding the foregoing provisions, if by reason of force majeure the District is unable in whole or in part to carry out its agreement on its part herein contained, other than the obligations on the part of the District contained in the Installment Sale Agreement, the District shall not be deemed in default during the continuance of such inability. The term "force majeure" as used means, without limitation, the following: acts of God; strikes, lockouts or other industrial disturbances; acts of public enemies; orders or restraints of any kind of the government of the United States of America or of the state wherein the District is located or any of their departments, agencies or officials, or any civil or military authority; insurrections; riots; landslides; earthquakes; fires; storms; droughts; floods; explosions; breakage or accident to machinery; or any other cause or event not reasonably within the control of the District.

Remedies on Default. Whenever any event of default referred to in paragraph (a), (c) or (e) above shall have happened and be continuing, the Trustee, as assignee of the Corporation, with the consent of the Bank and subject to the Installment Sale Agreement, shall proceed, or upon occurrence of an event of default specified in paragraph (b) or (d) above, may proceed, and upon written direction of the Bank or written request of the Owners of not less than a majority in aggregate principal amount of then Outstanding Certificates shall proceed to:

(a) declare the entire amount of Installment Payments then outstanding, including the Interest Components thereof then accrued and unpaid, immediately due and payable, without further demand;

(b) take whatever action, at law or in equity, may appear necessary or desirable to collect the Installment Payments and any other payments then due and thereafter to become due under the Installment Sale Agreement or to enforce the performance and observance of any obligation, covenant, agreement or provision contained in the Installment Sale Agreement to be observed or performed by the District; and

(c) take whatever other legal action may appear necessary or desirable to enforce its rights as assignee of the Corporation and the rights of the Owners of the Certificates.

Any such action by the Trustee, however, is subject to the condition that if, at any time after such action and before any judgment or decree for the payment of the moneys due shall have been obtained or entered, there shall be deposited with the Trustee a sum sufficient to pay all Installment Payments the payment of which is overdue, with interest on such overdue principal component of such overdue Installment Payments at the rate borne by the respective Certificates, and the reasonable charges and expenses of the Trustee, and any and all other defaults known to the Trustee (other than in the payment of the Installment Payments due and payable solely by reason of such action) shall have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate shall have been made therefor, then, and in every such case, the Owners of not less than a majority in aggregate principal amount with respect to the Certificates then Outstanding, by written notice to the District and the Trustee may, on behalf of the Owners of all of the Certificates, rescind and annul such action and its consequences and waive such default; but no such rescission and annulment shall extend to or shall affect any subsequent default, or shall impair or exhaust any right or power consequent thereon.

No Remedy Exclusive. No remedy conferred in the Installment Sale Agreement or reserved to the Corporation, the Bank or the Trustee is intended to be exclusive and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Installment Sale Agreement now or hereafter existing at law or in equity. No delay or omission to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver thereof, but any such right and power may be exercised from time to time and as often as may be deemed expedient. In order to entitle the Corporation or the Trustee to exercise any remedy reserved to it in the Installment Sale Agreement it shall not be necessary to give any notice, other than such notice as may be required in the Installment Sale Agreement.

Application of Moneys on Default. In the event of any default under the Installment Sale Agreement, moneys paid shall be applied as provided in the Trust Agreement.

#### AMENDMENTS TO INSTALLMENT SALE AGREEMENT

Amendments, Changes and Modifications. The Installment Sale Agreement and the rights and obligations of the District and the Corporation and of the Owners of the Certificates and of the Trustee may be modified or amended at any time by an amendment thereto which shall become binding when the written consents of the Owners of a majority in aggregate principal amount of the Certificates then Outstanding, exclusive of Certificates disqualified as provided in the Trust Agreement, and the written consent of the Bank shall have been filed with the Trustee. No such modification or amendment shall (1) extend the stated maturities of the Certificates, or reduce the rate of interest represented thereby, or extend the time of payment of interest, or reduce the amount of principal represented thereby, or reduce any premium payable on the prepayment thereof, without the consent of the Owner of each Certificate so affected, or (2) reduce the aforesaid percentage of Owners of Certificates whose consent is required for the execution of any amendment or modification of the Installment Sale Agreement, (3) modify any of the rights or obligations of the Trustee, the Bank or the Corporation without its written consent thereto, or (4) impair the right to tender Certificates pursuant to the Trust Agreement.

The Installment Sale Agreement and the rights and obligations of the District and the Corporation and of the Owners of the Certificates and of the Trustee may also be modified or amended at any time by an amendment thereto which shall become binding upon execution, without the consent of the Owners of any Certificates, but only to the extent permitted by law and only for anyone or more of the following purposes --

- (1) to add to the covenants and agreements of the District or the Corporation contained in the Installment Sale Agreement other covenants and agreements thereafter to be observed or to surrender any right or power herein reserved to or conferred upon the District or the Corporation, and which shall not adversely affect the interests of the Owners of the Certificates;

(2) to cure, correct or supplement any ambiguous or defective provision contained in the Installment Sale Agreement or in regard to questions arising under the Installment Sale Agreement, as the District or the Corporation may deem necessary or desirable and which shall not adversely affect the interests of the Owners of the Certificates;

(3) to make such other amendments or modifications as may be necessary in order to obtain a rating on the Certificates from S&P or any other national rating service; and

(4) with the written consent of the Bank, to make such other amendments or modifications as may be in the best interests of the Owners of the Certificates.

The District shall also obtain an Opinion of Bond Counsel.

Any provision of the Installment Sale Agreement expressly recognizing or granting rights in the Bank may not be amended in any manner which affects the rights of the Bank thereunder without the prior written consent of the Bank.

#### ASSIGNMENT; APPLICABLE LAW

Assignment by Corporation. The Corporation's right, title and interest in, to and under the Installment Sale Agreement, including all Installment Payments and payments of Additional Costs thereunder (except for the Corporation's right to indemnification), are assigned to the Trustee pursuant to the terms of the Trust Agreement concurrently with the execution and delivery of the Installment Sale Agreement. Upon assignment by the Corporation of its rights under the Installment Sale Agreement to the Trustee under the Trust Agreement, the Corporation shall be fully relieved of its obligation to perform any or all of the duties and obligations imposed upon Corporation (except for Corporation's obligations set forth in the Installment Sale Agreement).

Applicable Law. The Installment Sale Agreement shall be governed by and construed in accordance with the laws of the State of California.

**APPENDIX B**  
**DISTRICT AUDITED FINANCIAL STATEMENTS**

## **APPENDIX C**

### **ECONOMIC PROFILE FOR COUNTY OF SAN DIEGO**

#### **Introduction**

The County of San Diego is the southernmost major metropolitan area in the State of California. The County covers 4,255 square miles, extending 70 miles along the Pacific Coast from the Mexican border to Orange County, and inland 75 miles to Imperial County. Riverside and Orange Counties form the northern boundary. The County is approximately the size of the State of Connecticut.

The County is also growing as a major center for culture and education. Over 30 recognized art organizations including the San Diego Opera, the Old Globe Theater productions, the La Jolla Chamber Orchestra, as well as museums and art galleries, are located in the County. Higher education is provided through five two-year colleges and six four-year colleges and universities.

The San Diego Convention Center contains 361,000 square feet of exhibit space and over 100,000 square feet of meeting/banquet rooms. The Convention Center can accommodate events for 30,000-40,000 people.

In addition to the City of San Diego, other principal cities in the County include Carlsbad, Chula Vista, Oceanside, El Cajon, Escondido, La Mesa and National City. Most County residents live within 20 miles of the coast. Farther inland are agricultural areas, principally planted in avocados and tomatoes, while the easternmost portion of the County has a dry, desert-like topography.

## Population

The County has experienced rapid growth and development in the past 15 years. It has become the seventeenth most populous metropolitan area in the United States. The City of San Diego is the eighth most populous city in the United States. Total population for the County is expected to be over 3.63 million by the year 2015.

The following table shows the January 1 State of California Department of Finance estimates of total population in the San Diego region for each year since 2002, and the increase from the previous year.

TABLE NO. C-1  
COUNTY OF SAN DIEGO AND STATE OF CALIFORNIA  
POPULATION

Year	COUNTY OF SAN DIEGO		STATE OF CALIFORNIA	
	Population	Percentage Change	Population	Percentage Change
2002	2,920,566		35,063,959	1.7%
2003	3,071,494	1.7%	35,632,700	1.6%
2004	3,010,023	1.0%	36,199,342	1.6%
2005	3,039,424	1.0%	36,676,931	1.3%
2006	3,065,312	0.9%	37,087,005	1.1%
2007	3,096,975	1.0%	37,463,609	1.1%
2008	3,141,700	1.4%	37,871,509	1.0%
2009	3,185,467	1.4%	38,255,508	1.0%
2010	3,224,432	1.2%	38,648,000	1.7%
% Increase Between				
2002 - 2010		10.4%		10.2%

Source: State of California, Department of Finance, "E-4 Population Estimates for Cities, Counties and the State 2001-2010, with 2000 Benchmark."

## Per Capita Income

Per capita income information for the County, the State of California and the United States are summarized in the following table.

TABLE NO. C-2  
PER CAPITA INCOME  
SAN DIEGO COUNTY, STATE OF CALIFORNIA AND UNITED STATES  
2006 - 2010

Year	San Diego County	State of California	United States
2006	542,801	\$39,358	\$38,629
2007	44,832	41,571	38,615
2008	45,728	43,641	40,208
2009	43,285	(1)	(1)
2010	41,651	43,104	40,584

Source: County of San Diego, Comprehensive Annual Financial Report for the Year Ended June 30, 2010 and State of California Department of Finance; State of California Employment Development Department.

(1) Not Available.

## Employment

TABLE NO. C-3  
COUNTY OF SAN DIEGO, CALIFORNIA, AND UNITED STATES  
LABOR FORCE, EMPLOYMENT, AND UNEMPLOYMENT

Year and Area	Labor Force	Employment	Unemployment	Unemployment Rate
2006				
San Diego	1,499,900	1,440,400	59,400	4.0%
California	17,686,700	16,821,300	865,400	4.9
United States	151,413,000	144,419,000	7,001,000	4.6
2007				
San Diego	1,518,300	1,449,500	68,900	4.5
California	17,928,700	16,970,200	958,500	5.3
United States	153,126,000	146,049,000	7,078,000	4.6
2008				
San Diego	1,547,300	1,455,100	92,300	6.0
California	18,191,000	16,833,400	1,307,600	7.2
United States	154,329,000	145,368,000	8,924,000	5.8
2009				
San Diego	1,552,000	1,402,400	149,600	9.6
California	18,204,200	16,141,300	2,062,700	11.3
United States	154,142,000	139,877,000	14,265,000	9.3
2010				
San Diego	1,557,500	1,393,200	164,300	10.6
California	18,176,200	15,916,300	2,259,900	12.4
United States	(1)	(1)	(1)	(1)

Source: State of California Employment Development Department, Labor Market Information Division and United States Department of Labor, Bureau of Labor Statistics

(1) Not Available.

The District is located in the San Diego-Carlsbad-San Marcos Metropolitan Statistical Area (MSA). Six major job categories constitute 81.4% of the work force. They are government (18.4%), professional and business services (17.4%), service producing (13.6%), leisure and hospitality (12.5%), educational and health services (12.2%), and manufacturing (7.3%). The March 2011 unemployment rate in the San Diego-Carlsbad-San Marcos MSA was 10.2%. The State of California March 2011 unemployment rate (unadjusted) was 12.3%.

TABLE NO. C-4  
SAN DIEGO-CARLSBAD-SAN MARCOS MSA  
WAGE AND SALARY WORKERS BY INDUSTRY <sup>(1)</sup>  
(In thousands)

Industry	2007	2008	2009	2010	2011
Government	225.0	228.7	228.5	227.3	228.9
Other Services	48.2	48.5	47.3	46.7	46.2
Leisure and Hospitality	157.0	161.3	153.1	150.8	155.6
Educational and Health Services	128.7	135.7	144.6	146.8	151.7
Professional and Business Services	221.4	225.2	208.1	203.2	216.1
Financial Activities	81.9	76.6	71.7	67.2	66.9
Information	31.4	31.2	29.9	29.3	25.1
Transportation, Warehousing and Utilities	28.0	29.2	27.3	26.8	27.7
Service Producing					
Retail Trade	146.6	141.7	130.3	127.8	128.2
Wholesale Trade	45.3	45.0	41.4	38.7	40.1
Manufacturing					
Nondurable Goods	25.2	25.1	22.5	21.4	21.7
Durable Goods	77.5	77.9	76.3	71.1	70.1
Goods Producing					
Construction	88.3	77.9	63.9	55.0	54.0
Mining and Logging	0.4	0.4	0.4	0.4	0.4
Total Nonfarm	1,304.9	1,304.2	1,245.3	1,208.5	1,233.2
Farm	10.8	10.9	9.3	9.4	9.6
Total (all industries)	1,315.7	1,315.1	1,254.6	1,217.9	1,242.8

Source: State of California Employment Development Department, Labor Market Information Division, "Industry Employment & Labor Force - by month, March 2010 Benchmark."

<sup>(1)</sup> Annually, as of March

## Major Employers

The major employers operating within the County as of June 30, 2010 are shown in Table No. C-5.

**TABLE NO. C-5  
COUNTY OF SAN DIEGO  
MAJOR EMPLOYERS**

Employer	Number of Employees	Percent of Total Employment
Federal Government	44,000	3.13%
State of California	42,300	3.00
University of California, San Diego	26,823	1.91
County of San Diego	16,435	1.17
Sharp HealthCare	14,832	1.05
Scripps Health	13,823	0.98
Qualcomm Inc.	11,847	0.84
City of San Diego	10,470	0.74
Kaiser Permanente	7,404	0.53
U.S. Postal Service, San Diego District	6,080	0.43

Source: County of San Diego Comprehensive Annual Financial Report.

## **Transportation**

Excellent surface, sea and air transportation facilities service county residents and businesses. Interstate 5 parallels the coast from Mexico to the Los Angeles area and points north. Interstate 15 runs inland, leading to Riverside-San Bernardino, Las Vegas and Salt Lake City. Interstate 8 runs eastward through the southern United States.

San Diego's International Airport (Lindbergh Field) is located approximately one mile west of the downtown area at the edge of the San Diego Bay. The facilities are owned and maintained by the San Diego Unified Port District and are leased to commercial airlines and other tenants. The airport is the third most active commercial airport in California, served by 18 major airlines. In addition to San Diego International Airport, there are two naval air stations and seven general aviation airports located in the county.

San Diego is the terminus of the Santa Fe Railway's main line from Los Angeles. Amtrak passenger service is available at San Diego with stops at Del Mar and Oceanside in the north county. San Diego's harbor is one of the world's largest natural harbors. The harbor, a busy commercial port, has also become an extremely popular destination for cruise ships. The Port of San Diego is administered by the San Diego Unified Port District, which includes the cities of San Diego, National City, Chula Vista, Imperial Beach and Coronado.

## **Research and Development**

Research and development activity plays an important role in the area's economy. The County is a leading health sciences and biomedical center. Approximately 35,000 persons are engaged in life sciences-related activities in the metropolitan area, with over 28,000 employed directly in health services. In addition to the University of California San Diego campus, other established research institutions in the La Jolla area of the City include the Salk Institute for Biological Studies, the Scripps Clinic and Research Foundation, and the Scripps Institution of Oceanography.

## **Visitor and Convention Activity**

An excellent climate, proximity to Mexico, extensive maritime facilities, and such attractions as the San Diego Zoo and Wild Animal Park, Sea World, Cabrillo National Monument, and Palomar Observatory allow San Diego to attract visitor and convention business each year.

**APPENDIX D**  
**OPINION OF SPECIAL COUNSEL**

## APPENDIX E

### DTC AND THE BOOK-ENTRY-ONLY SYSTEM

*The following description of the Depository Trust Company (“DTC”), the procedures and record keeping with respect to beneficial ownership interests in the Certificates, payment of principal, interest and other payments on the Certificates to DTC Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in the Certificates and other related transactions by and between DTC, the DTC Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the DTC Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters, but should instead confirm the same with DTC or the DTC Participants, as the case may be.*

*Neither the issuer of the Certificates (the “Issuer”) nor the trustee, fiscal agent or paying agent appointed with respect to the Certificates (the “Agent”) take any responsibility for the information contained in this Appendix.*

*No assurances can be given that DTC, DTC Participants or Indirect Participants will distribute to the Beneficial Owners (a) payments of interest, principal or premium, if any, with respect to the Certificates, (b) certificates representing ownership interest in or other confirmation or ownership interest in the Certificates, or (c) redemption or other notices sent to DTC or Cede & Co., its nominee, as the registered owner of the Certificates, or that they will so do on a timely basis, or that DTC, DTC Participants or DTC Indirect Participants will act in the manner described in this Appendix. The current “Rules” applicable to DTC are on file with the Securities and Exchange Commission and the current “Procedures” of DTC to be followed in dealing with DTC Participants are on file with DTC.*

1. The Depository Trust Company (“DTC”), New York, NY, will act as securities depository for the securities (the “Securities”). The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Security certificate will be issued for each issue of the Securities, each in the aggregate principal amount of such issue, and will be deposited with DTC. If, however, the aggregate principal amount of any issue exceeds \$500 million, one certificate will be issued with respect to each \$500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such issue.

2. DTC, the world’s largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect

Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com) and [www.dtc.org](http://www.dtc.org). *The information contained on these Internet sites is not incorporated herein by reference.*

3. Purchases of Securities under the DTC system must be made by or through Direct Participants, which will receive a credit for the Securities on DTC’s records. The ownership interest of each actual purchaser of each Security (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Securities are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Securities, except in the event that use of the book-entry system for the Securities is discontinued.

4. To facilitate subsequent transfers, all Securities deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Securities with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Securities; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Securities are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

5. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Securities may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Securities, such as redemptions, tenders, defaults, and proposed amendments to the Security documents. For example, Beneficial Owners of Securities may wish to ascertain that the nominee holding the Securities for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

6. Redemption notices shall be sent to DTC. If less than all of the Securities within an issue are being redeemed, DTC’s practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

7. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Securities unless authorized by a Direct Participant in accordance with DTC’s MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.’s consenting or voting rights to those Direct Participants to whose accounts Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

8. Redemption proceeds, distributions, and dividend payments on the Securities will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC’s practice is to credit Direct Participants’ accounts upon DTC’s receipt of funds and corresponding detail information from Issuer or Agent, on payable date in accordance with their respective holdings shown on DTC’s records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in

bearer form or registered in “street name,” and will be the responsibility of such Participant and not of DTC, Agent, or Issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of Issuer or Agent, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to Issuer or Agent. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

10. Issuer may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered to DTC.

11. The information in this section concerning DTC and DTC’s book-entry system has been obtained from sources that Issuer believes to be reliable, but Issuer takes no responsibility for the accuracy thereof.

## APPENDIX F

### INFORMATION CONCERNING METROPOLITAN WATER DISTRICT'S WATER SUPPLY

The following information concerning the Metropolitan Water District's water supply is presented as general background data. MWD has entered into certain continuing disclosure agreements pursuant to which MWD is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 and annual audited financial statements (the "MWD Information") with the Municipal Securities Rulemaking Board which are available online at <http://emma.msrb.org>.

**MWD HAS NOT REVIEWED THIS OFFICIAL STATEMENT AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO MWD. MWD IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH MWD INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

MWD faces a number of challenges resulting from a combination of population growth, increased competition for low-cost water supplies, variable weather conditions and increased environmental regulations. MWD's resources and strategies for meeting these long-term challenges are set forth in its Integrated Water Resources Plan, as updated from time to time. See "*Integrated Water Resources Plan ("IRP") and Five-Year Supply Plan*" herein.

It is MWD's declared policy to meet all the supplemental needs of each of its member agencies, including SDCWA. However, MWD's Board adopted a shortage allocation method in February 2008 (the "Water Supply Allocation Plan"). The method allows MWD, in the event of shortages, to allocate water based on uniform reduction by class of water service, with adjustments made for growth, loss of local supply, demand hardening due to implementation of water conservation, and the amount a member agency's dependence on MWD for its total water supply, as well as other water supply related factors. MWD implemented the second stage of the shortage allocation method on July 1, 2009 and began allocating supplies among its member agencies pursuant to the plan. In April 2010, the MWD's Board adopted a resolution recognizing the continuing regional water shortage and again setting the shortage at the second stage of shortfall allocation, which sustained the prior year's regional water reduction of approximately 10%. Due to cool weather in the summer of 2010, impacts of the economic downturn and increased conservation, demand is expected to be less than the shortage allocation for 2010/11. Any extended curtailment could be accompanied by an increase in MWD water charges to its member agencies and consequently could necessitate an increase in water rates to the SDCWA member agencies, including the District.

#### **MWD Water Supply**

MWD's principal sources of water at the Colorado River and the State Water Project ("SWP").

##### Colorado River Water.

Under applicable laws, agreements and treaties governing the use of water from the Colorado River, California is apportioned the use of 4.4 million acre-feet of Colorado River water each year, plus one-half of any surplus that may be available for use collectively in Arizona, California and Nevada as declared on an annual basis by the United States Secretary of the Interior. Under the 1931 priority system that has formed the basis for the distribution of Colorado River water made available to California, MWD holds the fourth priority right of 550,000 acre-feet per year and a fifth priority right of 662,000 acre-feet per

year. MWD's fourth priority right is the last priority within California's basic annual apportionment of 4.4 million acre-feet; however, the fifth priority right is outside of this entitlement and therefore is not considered a firm supply of water. Until 2003, MWD had been able to take full advantage of its fifth priority right as a result of the availability of surplus water and apportioned but unused water. However, Arizona and Nevada have increased their use of water from the Colorado River, significantly reducing unused apportionment available for California since 2002. In addition, a severe drought in the Colorado River Basin reduced storage in system reservoirs, such that MWD stopped taking surplus deliveries in 2003 in an effort to mitigate the effects of the drought. Prior to 2003, MWD could divert over 1.2 million acre-feet in any year, but since that time, MWD's net diversions of Colorado River water have been limited to a low of approximately 633,000 acre-feet in 2006 and a high of approximately 1,105,232 acre-feet in 2009. Average annual net deliveries for 2003 through 2009 were approximately 813,800 acre-feet, with annual volumes dependent primarily on availability of unused higher priority agricultural water and increasing transfers of conserved water. In 2010, MWD's Colorado River Aqueduct deliveries are projected to reach 1.1 million acre-feet for the first time since 2002, including diversions from new programs and transactions under the *Five Year Supply Plan* and the *Quantification Settlement Agreement* ("QSA") described herein.

*Colorado River Aqueduct.* The Colorado River Aqueduct is owned and operated by MWD. Work on the Colorado River Aqueduct commenced in 1933 and water deliveries started in 1941. Additional facilities were completed by 1961 to meet additional requirements of MWD's member agencies. The Colorado River Aqueduct is 242 miles long, starting at Lake Havasu and terminating at Lake Mathews in Riverside County. After deducting for conveyance losses in transporting and storing the water and considering maintenance requirements, up to 1.25 million acre-feet per year may be conveyed through the Colorado River Aqueduct to MWD's member agencies, subject to the availability of Colorado River water.

*California's Colorado River Water Use Plan.* With Arizona's and Nevada's increasing use of their respective apportionments and the uncertainty of continued Colorado River surpluses, in 1997 the Colorado River Board of California, in consultation with MWD, Imperial Irrigation District ("IID"), Coachella Valley Water District ("CVWD"), the Palo Verde Irrigation District ("PVID"), the Los Angeles Department of Water and Power and the San Diego County Water Authority ("SDCWA"), developed a plan for reducing California's use of Colorado River water to its basic annual apportionment of 4.4 million acre-feet when use of that allotment is necessary (the "California Plan"). The May 2000 California Plan proposed to optimize the use of the available Colorado River supply through water conservation, transfers from higher priority agricultural users to MWD's service area and storage programs.

*Quantification Settlement Agreement.* Many of the core elements of the California Plan are being put into effect under the October 2003 Quantification Settlement Agreement (the "QSA") executed by CVWD, IID and MWD. The QSA establishes Colorado River water use limits for IID, CVWD and MWD, provides for specific acquisitions of conserved water and water supply arrangements for up to 75 years, and restores the opportunity for MWD to receive any "special surplus water" under the Interim Surplus Guidelines. See "*Interim Surplus Guidelines*" below. The QSA also allows MWD to enter into other cooperative Colorado River supply programs. Related agreements modify existing conservation and cooperative water supply agreements consistent with the QSA, and set aside several disputes among California's Colorado River water agencies.

Specific programs under the QSA include lining portions of the All-American and Coachella Canals, which are projected to conserve 96,000 acre-feet annually. As a result, 80,000 acre-feet of conserved water is projected to be delivered to SDCWA by exchange with MWD and 16,000 acre-feet is projected to be delivered for the benefit of the La Jolla, Pala, Pauma, Rincon and San Pasqual Bands of Mission Indians, the San Luis Rey Indian Water Authority, the City of Escondido and Vista Irrigation District, by exchange under a water rights settlement annually. An amendment to the IID-MWD 1988 Conservation Agreement and the associated 1989 Approval Agreement extended the term of the 1988 Conservation Agreement and limited the amount of water used by CVWD to 20,000 acre-feet. In 2021, the transfer of

water conserved annually by IID to SDCWA is expected to reach 205,000 acre-feet (see discussion below under the caption "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*"). With full implementation of the programs identified in the QSA, at times when California is limited to its basic apportionment of 4.4 million acre-feet per year, MWD expects to be able to annually divert to its service area approximately 850,000 acre-feet of Colorado River water plus any unused agricultural water that may be available. This is further augmented by the PVID program, which provides up to 129,800 acre-feet of water per year.

A complicating factor in completing the QSA was the fate of the Salton Sea. The Salton Sea is an important habitat for a wide variety of fish-eating birds as a stopover spot along the Pacific flyway. Some of these birds are listed as threatened or endangered species under the State and Federal endangered species acts ("ESAs"). Located at the lowest elevations of an inland basin and fed primarily by agricultural drainage with no outflows other than evaporation, the Salton Sea is trending towards hyper-salinity, which has already impacted the Salton Sea's fishery. This fishery has historically been suitable habitat for the fish-eating birds. The transfer of water from IID to SDCWA, one of the core programs implemented under the QSA, would reduce the volume of agricultural run-off from IID into the Salton Sea, which in turn would accelerate this natural trend of the Salton Sea to hyper-salinity. See "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*" below. The appropriate mitigation for impacts to the Salton Sea from the IID-SDCWA transfer and the larger issue of Salton Sea restoration was addressed by State legislation facilitating implementation of the QSA. In passing that legislation, the Legislature committed the State to undertake restoration of the Salton Sea ecosystem. Restoration of the Salton Sea is subject to selection and approval of an alternative by the Legislature and finding of the associated capital improvements and operating costs. The Secretary for the California Natural Resources Agency submitted an \$8.9-billion preferred alternative for restoration of the Salton Sea to the Legislature in May 2007. While withholding authorization of the preferred alternative, the Legislature has appropriated funds from Proposition 84 to undertake demonstration projects and investigations called for in the Secretary's recommendation. On September 25, 2010 Governor Schwarzenegger signed Senate Bill 51 establishing the "Salton Sea Restoration Council" as a state agency in the National Resources Agency to oversee restoration of the Salton Sea. The newly created Council was directed to evaluate alternative Sale Sea restoration plans, including those evaluated by the Secretary for the National Resources Agency, and to report to the Governor and Legislature by June 30, 2013 with a recommended Salton Sea restoration plan.

The QSA implementing legislation also established the Salton Sea Restoration Fund, which will be funded in part by payments made by the parties to the QSA and fees on certain water transfers among the parties to the QSA. Under the QSA agreements MWD will pay \$20 per acre-foot into the Salton Sea Restoration Fund for any special surplus Colorado River water that MWD elects to take under the Interim Surplus Guidelines. MWD also agreed to acquire up to 1.6 million acre-feet of water conserved by IID, excluding water transferred from IID to SDCWA (see "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*" below), if such water can be transferred consistent with plans for Salton Sea restoration, at an acquisition price of \$250 per acre-foot (in 2003 dollars), with net proceeds to be deposited into the Salton Sea Restoration Fund. No conserved water has been made available to MWD under this program. MWD may receive credit for the special surplus water payments against future contributions for the Lower Colorado River Multi-Species Conservation Program (see "*Environmental Considerations*" below). In consideration of these agreements, MWD will not have or incur any liability for restoration of the Salton Sea. As part of an effort to mitigate the effects of the drought in the Colorado River Basin that began in 2000, MWD elected not to take delivery of special surplus Colorado River water that was available from October 2003 through 2004 and from 2006 through 2007. No special surplus water has been available since 2007.

*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority.* On April 29, 1998, SDCWA and IID executed an agreement (the "Transfer Agreement") for SDCWA's purchase from IID of Colorado River water delivered to IID. An amended Transfer Agreement, executed as one of the QSA agreements, set the maximum transfer amount at 205,000 acre-feet in 2021, with the transfer

gradually ramping up to that amount over an approximately twenty-year period, stabilizing at 200,000 acre-feet per year beginning in 2023.

No facilities exist to deliver water directly from IID to SDCWA. Under the Transfer Agreement, conserved water from IID is delivered to SDCWA through existing facilities owned by MWD. MWD and SDCWA entered into an exchange contract that provides for conserved Colorado River water acquired by SDCWA from IID and water conserved from lining the All-American and Coachella Canals to be made available to MWD for diversion at Lake Havasu. By exchange from the sources of water available to MWD, an equal volume of water is delivered to SDCWA through MWD's distribution system. The price payable by SDCWA for these deliveries is calculated using the charges set by MWD's Board from time to time that are applicable to the conveyance of water by MWD on behalf of its member agencies.

*QSA Related Litigation.* On January 28, 2010, MWD was served with a complaint filed by the County of Imperial and the Imperial County Air Pollution Control District alleging that the execution and implementation of the QSA violates the National Environmental Policy Act and federal Clean Air Act. The complaint names the Department of Interior, Secretary of the Interior, Bureau of Reclamation and Commissioner of Reclamation as defendants, and MWD, CVWD, IID and SDCWA as real parties in interest. On March 29, 2010, MWD and the other defendants and real parties filed separate answers to the complaint. On August 23, 2010, MWD and the other real parties intervened as additional defendants. On September 9, 2010 the administrative record was filed with the court. A status conference was scheduled for December 9, 2010, at which time it is anticipated that a briefing schedule would be set. The impact, if any, that the litigation might have on MWD's water supplies cannot be adequately determined at this time.

On November 5, 2003, IID filed a validation action in Imperial County Superior Court, seeking a judicial determination that thirteen agreements associated with the IID/SDCWA water transfer and the QSA are valid, legal and binding. Other lawsuits also were filed challenging the execution, approval and subsequent implementation of the QSA on various grounds. All of the QSA cases were coordinated in Sacramento Superior Court. Between early 2004 and late 2009, a number of pretrial challenges and dispositive motions were filed by the parties and ruled on by the court, which reduced the number of active cases and narrowed the issues for trial, the first phase of which began on November 9, 2009 and concluded on December 2, 2009. One of the key issues in this first phase was the constitutionality of the QSA Joint Powers Agreement, pursuant to which IID, CVWD and SDCWA agreed to commit \$163 million toward certain mitigation and restoration costs associated with implementation of the QSA and related agreements, and the State agreed to be responsible for any costs exceeding this amount. A final judgment was issued on February 11, 2010, in which the court held that the State's commitment was unconditional in nature and, as such, violated the State's debt limitation under the California Constitution. The court also invalidated eleven other agreements, including the QSA, because they were inextricably interrelated with the QSA Joint Powers Agreement. Lastly, the court ruled that all other claims raised by the parties, including CEQA claims related to the QSA Programmatic EIR and the IID Transfer Project EIR, are moot. MWD, IID, CVWD, SDCWA, the State and others have appealed various aspects of the court's ruling, which has been stayed pending outcome of the appeal. If the ruling stands, it could delay the implementation of programs authorized under the QSA or result in increased costs or other adverse impacts. The impact, if any, that the ruling might have on MWD's water supplies cannot be adequately determined at this time.

The Navajo Nation has filed litigation against the Department of the Interior, specifically the Bureau of Reclamation and the Bureau of Indian Affairs, alleging that the Bureau of Reclamation has failed to determine the extent and quantity of the water rights of the Navajo Nation in the Colorado River and that the Bureau of Indian Affairs has failed to otherwise protect the interests of the Navajo Nation. The complaint challenges the adequacy of the environmental review for the Interim Surplus Guidelines (as defined under "*Interim Surplus Guidelines*" below) and seeks to prohibit the Department of the Interior from allocating any "surplus" water until such time as a determination of the rights of the Navajo Nation is completed. MWD has filed a motion to intervene in this action. In October 2004 the court granted the

motions to intervene and stayed the litigation to allow negotiations among the Navajo Nation, federal defendants, CAWCD, State of Arizona and Arizona Department of Water Resources. Recently the Navajo Nation approved the terms of a proposed settlement. Under its terms the Navajo would have specified rights to water from the Colorado River, the Little Colorado River and groundwater basins under the reservation. All Colorado River water would come from Arizona's apportionment. There would be no financial or water resource impact on MWD. The proposed agreement requires approval of all the affected bodies and federal implementing legislation. The litigation stay has been extended until April 13, 2011, to permit the parties to finalize the settlement. In the event the settlement is not finalized, the impact on MWD, if any, cannot be adequately determined at this time.

*Other MWD Colorado River Supply Programs.* MWD has taken steps to enhance its share of Colorado River water through agreements with other agencies that have rights to use such water such as IID, the PVID and the Central Arizona Water Conservation District.

*Interim Surplus Guidelines.* In January 2001, the Secretary of the Interior adopted guidelines (the "Interim Surplus Guidelines") for use through 2016 in determining if there is surplus Colorado River water available for use in California, Arizona and Nevada. The purpose of the Interim Surplus Guidelines is to provide a greater degree of predictability with respect to the availability and quantity of surplus water through 2016. The Interim Surplus Guidelines were later extended through 2026. The Interim Surplus Guidelines contain a series of benchmarks for reductions in agricultural use of Colorado River water within California by set dates.

Under the Interim Surplus Guidelines, MWD initially expected to divert up to 1.25 million acre-feet of Colorado River water annually under foreseeable runoff and reservoir storage scenarios from 2004 through 2016. However, an extended drought in the Colorado River Basin reduced these initial expectations. From 2000 to 2004, snow pack and runoff in the Colorado River Basin were well below average. Although runoff was slightly above average in 2005 and 2008, average annual runoff from 2000 through 2010 was 69% of normal, representing the driest eleven-year period on record. As of November 2010, combined storage in Lake Mead and Lake Powell was at 50 percent of capacity. Lake Mead's elevation had dropped to 1,082 feet above sea level, the lowest elevation since 1937. Lake Powell was at 63 percent of capacity, with 2010 water year runoff above Lake Powell at 72 percent of average.. MWD's initial 2010 diversion approval from the Bureau of Reclamation totaled 935,700 acre-feet plus any unused Priority 1 through 3 water. MWD anticipates its ultimate 2010 diversion approval from the Bureau of Reclamation will be approximately 1.1 million acre-feet.

SNWA and MWD entered into an Agreement Relating to Implementation of Interim Colorado River Surplus Guidelines on May 16, 2002, in which SNWA and MWD agreed to the allocation of unused apportionment as provided in the Interim Surplus Guidelines and on the priority of SNWA for interstate banking of water in Arizona. SNWA and MWD entered into a storage and interstate release agreement on October 21, 2004. Under this program, Nevada can request that MWD store unused Nevada apportionment in California. The amount of water stored through 2009 under this agreement was 70,000 acre-feet. In subsequent years, Nevada may request recovery of this stored water. As part of a recently executed amendment, it is expected that Nevada will not request return of this water until 2022. The stored water provides flexibility to MWD for blending Colorado River water with State Water Project water and improves near-term water supply reliability.

*Lower Basin Shortage Guidelines and Coordinated Management Strategies for Lake Powell and Lake Mead.* In November 2007, the Bureau of Reclamation issued a Final Environmental Impact Statement ("EIS") regarding new federal guidelines concerning the operation of the Colorado River system reservoirs. These new guidelines provide water release criteria from Lake Powell and water storage and water release criteria from Lake Mead during shortage and surplus conditions in the Lower Basin, provide a mechanism for the storage and delivery of conserved system and non-system water in Lake Mead and extend the Interim Surplus Guidelines through 2026. The Secretary of the Interior issued the final guidelines through a Record of Decision signed in December 2007. The Record of Decision and

accompanying agreement among the Colorado River Basin States protect reservoir levels by reducing deliveries during drought periods, encourage agencies to develop conservation programs and allow the states to develop and store new water supplies. The Colorado River Basin Project Act of 1968 insulates California from shortages in all but the most extreme hydrologic conditions.

*Environmental Considerations.* Several fish species and other wildlife species either directly or indirectly have the potential to affect Colorado River operations, thus changing power operations and the amount of water deliveries to the Colorado River Aqueduct. A number of species that are on either “endangered” or “threatened” lists under the federal and/or California ESAs are present in the area of the Lower Colorado River. To address this issue, a broad-based state/federal/tribal private regional partnership, which includes water, hydroelectric power and wildlife management agencies in Arizona, California and Nevada, developed a multi-species conservation plan for the main stem of the Lower Colorado River (the Lower Colorado River Multi-Species Conservation Program or “MSCP”). The MSCP allows MWD to obtain federal and state permits for any incidental take of protected species resulting from current and future water and power operations and to minimize any uncertainty from additional listings of endangered species. The MSCP also covers operations of federal dams and power plants on the Colorado River.

*Seismic Considerations.* MWD’s water conveyance and distribution facilities are designed to either withstand a maximum probable seismic event or to minimize the potential repair time in the event of damage. The five pumping plants on the Colorado River Aqueduct have been buttressed to better withstand seismic events. Other components of the Colorado River Aqueduct are monitored for any necessary rehabilitation and repair. Supplies are dispersed throughout Metropolitan’s service area, and a six-month reserve supply of water normally held in local storage (including emergency storage in Diamond Valley Lake) provides reasonable assurance of continuing water supplies during such events. However, major portions of the California Aqueduct, the Colorado River Aqueduct and MWD’s internal distribution system are located near major earthquake faults, including the San Andreas Fault. A significant earthquake could damage project structures and interrupt the supply of water.

#### State Water Project.

MWD’s other major source of water is the State Water Project (“SWP”). The SWP is owned by the State of California and operated by the California Department of Water Resources (“DWR”). The SWP transports Feather River water stored in and released from Oroville Dam and unregulated flows diverted directly from the San Francisco Bay/Sacramento-San Joaquin Delta Estuary (“Bay-Delta”) south via the California Aqueduct to four delivery points near the northern and eastern boundaries of MWD. The total length of the California Aqueduct is 444 miles.

MWD is one of 29 agencies that have long-term contracts for water service from DWR, and is the largest agency in terms of the number of people it serves (almost 19 million), the share of SWP water to which it has contracted to receive (approximately 46%), and the percentage of total annual payments made to DWR (approximately 58% in 2009). Upon expiration of the State Water Contract term (currently 2035), MWD has the option to continue service under substantially the same terms and conditions. MWD presently intends to exercise this option to at least 2052.

The SWP was originally intended to meet demands of 4.2 million acre-feet per year. Initial SWP facilities were completed in the early 1970’s, and it was envisioned that additional facilities would be constructed as contractor demands increased. Several factors, including public opposition, increased costs, and increased non-SWP demands for limited water supplies, combined to delay the construction of additional facilities. The quantity of SWP water available for delivery each year is controlled by both hydrology and operational considerations. Under a 100% allocation, the State Water Contract provides MWD with 1,911,500 acre-feet of water. Water received from the SWP by MWD over the eight years from 2002 through 2009, including water from water transfer, groundwater banking and exchange programs varied from a low of 908,000 acre-feet in calendar year 2009 to a high of 1,800,000 acre-feet in calendar year 2004. For calendar year 2009, DWR’s allocation to SWP contractors was 40% of contracted amounts,

reflecting low water storage in the State's major reservoirs, below-normal runoff and regulatory restrictions on water exports from the Bay-Delta to protect listed fish species. Under the 40% allocation, MWD received 765,000 acre-feet from its basic allocation, with 908,000 acre-feet of total water delivered from the SWP in 2009, including supplies from water transfers, exchanges and related Five-Year Supply Plan actions delivered through the California Aqueduct.

For calendar year 2010, DWR's initial allocation estimate to SWP contractors was set at five percent of contracted amounts. The estimate was adjusted upwards during the winter and spring and on June 22, 2010, DWR adjusted its allocation to 50 percent of contracted amounts, reflecting late spring storms, a return to normal precipitation and reservoir levels and an above normal Sierra snowpack. For MWD, the revised allocation provides 955,750 acre-feet, or 50 percent of its 1,911,500-acre-foot contractual amount. The allocation is based on SWP yields under pumping restrictions due to the biological opinions for Delta smelt and Chinook salmon. For 2010, MWD projected delivery of 1,160,000 acre-feet to its service area plus approximately 180,000 acre-feet of net deliveries to storage in its Central Valley groundwater storage programs. This includes SWP supplies from water transfers, exchanges and related Five-Year Supply Plan actions delivered through the California Aqueduct.

On December 16, 2010, DWR's initial calendar year 2011 allocation estimate of water from the SWP was increased from 25 percent to 50 percent of SWP contractors' contractual amounts. For MWD, the revised allocation is 955,750 acre-feet, or 50 percent of its 1,911,500 acre-foot contractual amount. This revised 50 percent allocation for 2011, due to fall 2010 storms and improved carryover levels in the state's major reservoirs, is much improved from the previous year's initial five percent allocation and the highest early season water supply outlook in four years. DWR stated that its allocation is a conservative estimate of what DWR expects it can deliver as a percentage of deliveries requested by SWP contractors for 2011. Actual deliveries and revised allocations for 2011 are expected to increase during the year once actual hydrologic and water supply conditions are known.

Due to drought conditions and the court-ordered restrictions described under "*Endangered Species Act Considerations*" below, California Governor Arnold Schwarzenegger issued a proclamation on February 27, 2009 declaring a statewide drought emergency. The proclamation requested that all urban water users in California increase water conservation and directed that various state agencies take action to address impacts of the drought. These actions included expediting approvals for water transfers (provided that such transfers do not injure other legal users of water or unreasonably affect fish and wildlife); pursuing short-term efforts, such as installation of temporary barriers in the Bay-Delta, to protect water quality and water supply; and expediting regulatory consideration of proposed modifications to Bay-Delta water quality standards. Although cold Pacific storms in April and May 2010 significantly improved water supply outlook conditions, as of November 1, 2010, DWR has classified the water year as below normal and the statewide drought emergency was still in effect. [to be updated]*Bay-Delta Regulatory and Planning Activities*. The State Water Resources Control Board ("SWRCB") is the agency responsible for setting water quality standards and administering water rights throughout California. Decisions of SWRCB can affect the availability of water to MWD and other users of SWP water. SWRCB exercises its regulatory authority over the Bay-Delta by means of public proceedings leading to regulations and decisions. These include the Bay Delta Water Quality Control Plan ("WQCP"), which establishes the water quality standards and proposed flow regime of the estuary, and water rights decisions which assign responsibility for implementing the objectives of the WQCP to users throughout the system by adjusting their respective water rights. Since 2000, SWRCB's Water Rights Decision 1641 has governed the SWP's ability to export water from the Bay-Delta for delivery to MWD and other SWP contractors.

The CALFED Bay-Delta Program is a collaborative effort among state and federal agencies to improve water supplies in California and the health of the Bay-Delta watershed. In August 2000, the federal government and the State of California issued a Record of Decision ("ROD") and related documents approving the final programmatic environmental documentation for the CALFED Bay-Delta Program.

Implementing the CALFED Bay-Delta Program has resulted in investment of \$3 billion on a variety of projects and programs to begin addressing the Bay-Delta's water supply, water quality, ecosystem, and levee stability problems. To guide future development of the CALFED Bay-Delta Program and identify a strategy for managing the Bay-Delta as a sustainable resource, Governor Schwarzenegger in September 2006 established, by Executive Order, a Delta Vision process. The Delta Vision process is tied to legislation that created a cabinet-level committee tasked with developing a strategic vision for the Delta. The 41-member Delta Vision Blue Ribbon Task Force issued its Delta Vision Strategic Plan (the "Strategic Plan") on October 17, 2008, providing its recommendations for long-term sustainable management of the Bay-Delta. The Strategic Plan was reviewed by the Delta Vision Committee, chaired by the State Secretary for Resources. The Implementation Report summarizing the Delta Vision Committees recommendations was submitted to Governor Schwarzenegger on December 31, 2008. These recommendations include completing the BDCP and associated environmental assessments to permit ecosystem revitalization and conveyance water improvements, identifying and reducing stressors to the Bay-Delta ecosystem, strengthening levees, increasing emergency preparedness, continuing finding for the CALFED ecosystem restoration program, updating Bay-Delta regulatory flow and water quality standards to protect beneficial uses of water and working with the State Legislature on a comprehensive water bond package to fund Bay-Delta infrastructure projects.

On November 4, 2009, the State Legislature authorized an \$11.1 billion water bond measure that includes over \$2 billion for Bay-Delta ecosystem restoration, as well as \$3 billion for new water storage and additional funds for water recycling, drought relief, conservation and watershed projects. The bonds are subject to voter approval and were scheduled to be included on the November 2010 ballot; however, in August 2010, the Legislature postponed the bond election to 2012. Related legislation created a new oversight council for the Bay-Delta and directs that the Bay-Delta be managed with the dual goals of water supply reliability and ecosystem protection, sets a statewide conservation target for urban per capita water use of 20% reductions by 2020, provides funding for increase enforcement of illegal water diversions and establishes a statewide groundwater monitoring program.

*Endangered Species Act Considerations.* The listing of several fish species as threatened or endangered under the federal or California Endangered Species Acts (respectively, the "Federal ESA" and the "California ESA" and, collectively, the "ESAs") have adversely impacted SWP operations and limited the flexibility of the SWP. Currently, five species (the winter-run and spring-run Chinook salmon, Delta smelt, North American green sturgeon and Central Valley steelhead) are listed under the ESAs. In addition, on June 25, 2009, the California Fish and Game Commission declared the longfin smelt a threatened species under the California ESA. The United States Fish and Wildlife Service ("USFWS") announced on April 9, 2009, that the Bay-Delta population of longfin smelt does not qualify as a distinct population segment and cannot be listed under the Federal ESA.

The Federal ESA requires that before any federal agency authorizes finds or carries out an action it must consult with the appropriate federal fishery agency to determine whether the action would jeopardize the continued existence of any threatened or endangered species, or adversely modify habitat critical to the species' needs. The result of the consultation is known as a "biological opinion." In the biological opinion the federal fishery agency determines whether the action would cause jeopardy to a threatened or endangered species or adverse modification to critical habitat and recommends reasonable and prudent alternatives or measures that would allow the action to proceed without causing jeopardy or adverse modification. The biological opinion also includes an "incidental take statement." The incidental take statement allows the action to go forward even though it will result in some level of "take," including harming or killing some members of the species, incidental to the agency action, provided that the agency action does not jeopardize the continued existence of any threatened or endangered species and complies with reasonable mitigation and minimization measures recommended by the federal fishery agency.

In 2004 and 2005, the USFWS and National Marine Fisheries Service ("NMFS") issued biological opinions and incidental take statements that govern operations of the SWP and the federal Central Valley Project (the "CVP") with respect to the Delta smelt, the winter-run and spring-run Chinook salmon and

the Central Valley steelhead. In July 2006, the Bureau of Reclamation reinitiated consultation with the USFWS and NMFS with respect to the 2004 and 2005 biological opinions (with the addition of the North American green sturgeon, which was listed in April 2006) following the filing of legal challenges to those biological opinions and incidental take statements described under —*Federal ESA Litigation* below. In a separate action on June 2, 2010, the National Marine Fisheries Service published regulations under the Federal ESA, applying Federal ESA “take” prohibitions to the North American green sturgeon. Existing restrictions on project operations for the benefit of other listed species will also protect the North American green sturgeon and it is unclear whether additional restrictions and impacts on project operations could result from the rule. Under the Federal ESA, critical habitat must also be designated for each listed species. Critical habitat has been designated for each of the currently listed species, including the North American green sturgeon. The NMFS issued critical habitat designation for the North American green sturgeon on October 9, 2009. The habitat designated as critical for the sturgeon includes the lower Feather River, which could have an adverse impact on SWP operations. The extent of any such impacts cannot be determined at this time.

Litigation filed by several environmental interest groups (*NRDC v. Kempthorne*; and *Pacific Coast Federation of Fishermen’s Associations v. Gutierrez*) in the United States District Court for the Eastern District of California alleged that the 2004 and 2005 biological opinions and incidental take statements inadequately analyzed impacts on listed species under the Federal ESA. On May 25, 2007, Federal District Judge Wanger issued a decision on summary judgment in *NRDC v. Kempthorne*, finding the USFWS biological opinion for Delta smelt to be invalid. On December 14, 2007, Judge Wanger issued his Interim Remedial Order and Findings of Fact and Conclusions of Law requiring that the State Water Project and Central Valley Project operate according to certain specified criteria until a new biological opinion for the Delta smelt is issued. Under the Interim Remedial Order, SWP operations were constrained in the winter and spring of 2007/08 by prevailing conditions and the status of the Delta smelt. The USFWS released a new biological opinion on the impacts of the SWP and CVP on Delta smelt on December 15, 2008. MWD, the San Luis & Delta Mendota Water Authority, Westlands Water District, Kern County Water Agency, Coalition for a Sustainable Delta and State Water Contractors, a California nonprofit corporation formed by agencies contracting with DWR for water from the State Water Project (the “State Water Contractors”), the Family Farm Alliance and the Pacific Legal Foundation on behalf of several owners of small farms in California’s Central Valley have filed separate lawsuits in federal district court challenging the biological opinion. MWD’s lawsuit challenging the biological opinion alleges, among other things, that the biological opinion is unlawful and invalid because it failed to use the best available scientific data and information and that the “Reasonable and Prudent Alternative” in the biological opinion, which imposes major water export restrictions, was arbitrary and capricious, and lacked necessary findings. The federal court has consolidated the six lawsuits challenging the Delta smelt biological opinion under the caption *Delta Smelt Consolidated Cases*. The briefings and hearings on motions in these cases and the *Consolidated Salmon Cases* are described below.

On April 16, 2008, in *Pacific Coast Federation of Fishermen’s Associations v. Gutierrez* the court invalidated the 2004 NMFS’s biological opinion for the salmon and other fish species that spawn in rivers flowing into the Bay-Delta. Among other things, the court found that the no jeopardy conclusions in the biological opinion were inconsistent with some of the factual findings in the biological opinion; that the biological opinion failed to adequately address the impacts of SWP and CVP operations on critical habitat and that there was a failure to consider how climate change and global warming might affect the impacts of the projects on salmonid species. The NMFS released its new biological opinion for salmonid species on June 4, 2009. The salmonid species biological opinion contains additional restrictions on SWP and CVP operations. The NMFS calculated that these restrictions will reduce the amount of water the SWP and CVP combined will be able to export from the Bay-Delta by 5 to 7%. DWR estimated a 10% average water loss, expected to begin in 2010, under this biological opinion. See “*State Water Project Operational Constraints*” below for the estimated impact to MWD’s water supply. Six lawsuits have been filed challenging the 2009 salmon biological opinion. These various lawsuits have been brought by the San Luis & Delta Mendota Water Authority, Westlands Water District, Stockton East Water District, Oakdale Irrigation District, Kern County Water Agency, the State Water Contractors and MWD. The

court has consolidated the cases under the caption *Consolidated Salmon Cases*. On May 25, 2010, the court granted the plaintiffs' request for preliminary injunction in the *Consolidated Salmon Cases*, restraining enforcement of two requirements under the salmon biological opinion that limit exported water during the spring months based on San Joaquin River flows into the Bay Delta and reverse flows on the Old and Middle Rivers. On May 27, 2010, the court ruled in the *Delta Smelt Consolidated Cases* that the plaintiffs had established legal and equitable grounds for injunctive relief against enforcement of a similar limitation of reverse flows on the Old and Middle Rivers during the spring months under the Delta smelt biological opinion, but could not enjoin the limitation absent a showing that the Delta smelt are not within imminent risk of entrainment by the projects' pumps. The court deferred issuance of a preliminary injunction while the parties negotiated a compromise for June 2010 project operations. Hearings on motions for summary judgment in the *Delta Smelt Consolidated Cases* were held on July 8 and 9, 2010. On December 14, 2010, Judge Wanger issued a decision on summary judgment in the *Delta Smelt Consolidated Cases* finding that there were major scientific and legal flaws in the Delta smelt biological opinion, and remanding the biological opinion to the USFWS for reconsideration. The court's decision invalidates some of the restrictions on project operations contained in the Delta smelt biological opinion. The court scheduled a hearing on January 4, 2011 to determine what additional steps should be taken in the litigation. [At that time, the court may schedule an interim remedies proceeding to determine how the projects should be operated while the Delta smelt biological opinion is being reconsidered. *update*] Any interim operational restrictions on the projects, and how they may affect MWD's SWP water supply, are unknown. Hearings on motions for summary judgment in the *Consolidated Salmon Cases* commenced on December 16. It is unknown when the court will issue a decision in the *Consolidated Salmon Cases*. On November 13, 2009, the Center for Biological Diversity filed separate lawsuits challenging the USFWS' failure to respond to a petition to change the Delta smelt's federal status from threatened to endangered and the USFWS' denial of federal listing for the longfin smelt. The Delta smelt and longfin smelt cases were filed in the United States District Court for the Eastern and Northern Districts of California, respectively.

*State Water Project Operational Constraints.* DWR has altered the operations of the SWP to accommodate species of fish listed under the ESAs. These changes in project operations have adversely affected SWP deliveries. Restrictions on Bay-Delta pumping under the Interim Remedial Order in *NRDC v. Kempthorne* reduced deliveries of SWP water to MWD by approximately 250,000 acre-feet in 2008 and 199,000 acre-feet in 2009. The impact on total SWP deliveries attributable to the Delta smelt and salmonid species biological opinions combined is estimated to be one million acre-feet in an average year, reducing SWP deliveries from approximately 3.3 million acre-feet to approximately 2.3 million acre-feet for the year under average hydrology. Reductions to SWP total deliveries from the biological opinions are estimated to range from 0.3 million acre-feet during critically dry years to 1.3 million acre-feet in above normal water years. MWD received approximately 908,000 acre-feet of total water deliveries from the SWP in 2009, including its basic allocation and supplies from water transfers, exchanges and related Five-Year Supply Plan actions that will be delivered through the California Aqueduct. The initial allocation to SWP contractors for 2010 was only 5% of their contracted amounts, based on below-average precipitation and regulatory agency restrictions on water exports from the Bay-Delta to protect listed fish species. DWR revisited this allocation as conditions changed, and on June 22, 2010, announced a final allocation of 50% (955,750 acre-feet for MWD). The allocation incorporates anticipated impacts of pumping restrictions due to the biological opinions for Delta smelt and Chinook salmon on SWP yields. On August 24, 2010, DWR reported that approximately 800,000 acre-feet of water was lost from the SWP for calendar year 2010 as a result of pumping restrictions, of which about 370,000 acre-feet would have been made available to MWD.

Operational constraints likely will continue until a long-term solution to the problems in the Bay-Delta is identified and implemented. The Delta Vision process, established by Governor Schwarzenegger, is aimed at identifying long-term solutions to the conflicts in the Bay-Delta, including natural resource, infrastructure, land use and governance issues. In addition, State and federal resource agencies and various environmental and water user entities are currently engaged in the development of the Bay-Delta

Conservation Plan, which is aimed at addressing ecosystem needs and securing long-term operating permits for the SWP.

Other issues, such as the recent decline of some fish populations in the Bay-Delta and surrounding regions and certain operational actions in the Bay-Delta, may significantly reduce MWD's water supply from the Bay-Delta. SWP operational requirements may be further modified under new biological opinions for listed species under the Federal ESA or by the California Department of Fish and Game's issuance of incidental take authorizations under the California ESA. Biological opinions or incidental take authorizations under the Federal ESA and California ESA might further adversely affect SWP and CVP operations. Additionally, new litigation, listings of additional species or new regulatory requirements could further adversely affect SWP operations in the future by requiring additional export reductions, releases of additional water from storage or other operational changes impacting water supply operations. MWD cannot predict the ultimate outcome of any litigation or regulatory process described above, but believed they could have a materially adverse impact on the operation of SWP pumps, MWD's SWP supplies and MWD's water resources.

*Integrated Water Resources Plan ("IRP") and Five-Year Supply Plan.* MWD, its member agencies, sub-agencies and groundwater basin managers developed the IRP that was adopted by the MWD Board in January 1996 as a long-term planning guideline for resources and capital investments. The purpose of the IRP was the development of a preferred resource mix to meet the water supply reliability and water quality needs for the region in a cost effective and environmentally sound manner. This plan was updated in 2004. On October 12, 2010, MWD's Board adopted an IRP update (the "2010 IRP Update") as a strategy to set goals and a framework for water resources development. This strategy enables MWD and its member agencies to manage future challenges and changes in California's water conditions and to balance investments with water reliability benefits. The 2010 IRP Update was formulated with input from member agencies, retail water agencies, and other stakeholders including water and wastewater managers, environmental and business interests and the community. The framework places an emphasis on regional collaboration. The 2010 IRP Update seeks to provide regional flexibility through 2035 by stabilizing MWD's traditional imported water supplies and continuing to develop additional local resources. It also advances long-term planning for potential future contingency resources, such as storm water capture and large-scale seawater desalination, in close coordination with MWD's 26 member agencies and other utilities. The 2010 IRP Update is available on MWD's website. Specific projects that may be developed by MWD in connection with the implementation of the IRP will be subject to future Board consideration and approval, as well as environmental and regulatory documentation and compliance. The information set forth on MWD's web site is not incorporated by reference.

In April 2008, MWD staff began working with MWD's member agencies on a Five-Year Supply Plan to identify specific resource and conservation actions over a five year period, in order to manage water deliveries under continued drought conditions and court-ordered restrictions. The Five-Year Supply Plan focuses on six categories of resource options to improve MWD's reliability from 2010 through 2014. These categories are (1) water conservation, (2) Colorado River transactions, (3) near-term Delta actions, (4) SWP transactions, (5) groundwater recovery, and (6) local resources. The Water Supply Allocation Plan was approved by the MWD Board in February 2008. The Water Supply Allocation Plan provides a formula for equitable distribution of available supplies in case of extreme water shortages within Metropolitan's service area. On April 14, 2009, MWD's Board adopted a resolution declaring a regional water shortage and implementing the Water Supply Allocation Plan, effective July 1, 2009. The Board set the "Regional Shortage Level" at Water Supply Allocation Plan Level 2, which required reduction of regional water use by approximately 10% and resulted in the sale of about 1.89 million acre-feet of MWD water in fiscal year 2009/10. The final 2009/10 allocation for each member agency was dependent upon its local production during the allocation year and determined through a formal local supply certification process with the member agencies. On April 13, 2010, the MWD Board adopted a resolution recognizing the continuing regional water shortage and again setting the Regional Shortage Level at Water Supply Allocation Plan Level 2, which sustains the prior year's regional water use reduction of approximately 10 percent. As of November 2010, the water supply allocation allows for the sale of about 2.12 million acre-

feet of MWD water in fiscal year 2010/11 for municipal and industrial, Interruptible Agricultural Water Program and seawater barrier deliveries. Due to cool weather in summer 2010, impacts of the economic downturn and increased conservation, fiscal year 2010/11 sales are forecasted as of November 2010 to be below the allocated amount of 2.12 million acre-feet of MWD water. The reduced demands allow for additional storage and, if current trends continue, will allow MWD to store approximately 650,000 acre-feet in 2010.

*Additional MWD Water Supply Enhancements.* MWD is currently pursuing voluntary water transfer and storage and exchange programs with the State, federal, public and private water districts and individuals. MWD has entered into groundwater basin storage agreements with the Arvin-Edison Water Storage District and the Semitropic Water Storage District, an agreement with San Bernardino Valley Municipal Water District to coordinate the use of facilities and SWP supplies and groundwater banking and exchange transfer agreements with the Kern Delta Water District and the Mojave Water Agency. MWD has also entered into an agreement with DWR to purchase a portion of the water released by the Yuba County Water Agency, and has been negotiating water purchase, storage and exchange programs with other agencies in the Sacramento and San Joaquin Valleys. MWD also has an exchange transfer and delivery agreement with the CVWD and the Desert Water Agency.

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**FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT**

by and between

**OTAY WATER DISTRICT**

and

**OTAY SERVICE CORPORATION**

**Dated as of June 1, 2011**

**Relating to**

**OTAY WATER DISTRICT**

**\$15,400,000**

**VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION  
(1996 CAPITAL PROJECTS)**

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## FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT

THIS FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT (the "First Amendment") is dated as of June 1, 2011, by and between the OTAY WATER DISTRICT, a municipal water district organized and existing under the laws of the State of California (the "District"), and the OTAY SERVICE CORPORATION, a nonprofit public benefit corporation existing under the laws of the State of California (the "Corporation"), and amends, in part, the Installment Sale Agreement dated as of June 1, 1996 by and between the District and the Corporation (the "Original Installment Sale Agreement").

### *WITNESSETH:*

WHEREAS, in connection with the execution and delivery of the Original Installment Sale Agreement, the District, the Corporation and The Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") entered into that certain Trust Agreement dated as of June 1, 1996 pursuant to which the Otay Water District Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates") were executed and delivered; and

WHEREAS, the existing Facility securing the repayment of the Certificates under the Trust Agreement is expiring and will not be renewed; and

WHEREAS, in accordance with the provisions of Section 5.06 of the Trust Agreement the District desires to cause a Substitute Facility from Union Bank, N.A. to be delivered to the Trustee to replace the existing letter of credit; and

WHEREAS, the expiration of the existing Facility will result in a mandatory tender of the Certificates under the terms of the Trust Agreement on June 3, 2011 (the "Mandatory Tender Date"); and

WHEREAS, the District and the Corporation have determined that the amendments set forth herein are desirable and may be made with the consent of the Bank and the Remarketing Agent, acting in its capacity as the owner of the Certificates on the Mandatory Tender Date ; and

WHEREAS, all acts, conditions and things required by law to exist, to have happened and to have been performed precedent to and in connection with the execution and delivery of this First Amendment do exist, have happened and have been performed in regular and due time, form and manner as required by law, and the parties hereto are now duly authorized to execute and enter into this First Amendment;

NOW, THEREFORE, in consideration of the covenants and provisions herein set forth and for other valuable consideration the receipt and sufficiency of which is hereby acknowledged, the parties hereto do hereby agree as follows:

**Section 1. Amendment of Section 1.01.** Section 1.01 of the Original Installment Sale Agreement is amended, in part, by deleting the defined terms "Custody Agreement," "Information

Services,” “Letter of Credit,” Operation and Maintenance Expenses,” “Remarketing Agreement,” and “Termination Date” and adding the following definitions to Section 1.01 to read as follows:

“Bonds” means all revenue bonds or notes of the District authorized, executed, issued and delivered by the District, the payments of which are on a parity with the Installment Payments and which are secured by a pledge of and lien on the Taxes and Revenues.

“Custody Agreement” means the Custody Agreement dated as of June 1, 2011, between the Custody Agent and the Bank related to Bank Certificates and any similar agreement between the Custody Agent and a Bank providing a Substitute Facility.

“Contracts” means this Installment Sale Agreement and any amendments and supplements hereto, and all contracts of the District authorized and executed by the District, payments under which are on a parity with the Installment Payments and which are secured by a pledge of and lien on the Taxes and Revenues.

“Debt Service” means, for any Fiscal Year, the sum of:

(1) the interest accruing during such Fiscal Year on all outstanding Bonds, assuming that all outstanding serial Bonds are retired as scheduled and that all outstanding term Bonds are prepaid or paid from sinking fund payments as scheduled (except to the extent that such interest is capitalized);

(2) that portion of the principal amount of all outstanding serial Bonds maturing in such Fiscal Year or maturing in the next succeeding Fiscal Year accruing during such Fiscal Year in each case computed as if such principal amounts were deemed to accrue daily during such Fiscal Year in equal amounts;

(3) that portion of the principal amount of all outstanding term Bonds required to be prepaid or paid in such Fiscal Year or during the next succeeding Fiscal Year in each case computed as if such principal amounts were deemed to accrue daily during such Fiscal Year in equal amounts; and

(4) that portion of the installment payments required to be made during such Fiscal Year or during the next succeeding Fiscal Year under all Contracts, in each case computed as if such installment payments were deemed to accrue daily during such Fiscal Year in equal amounts (except to the extent that the interest portion of such installment payments is capitalized);

less the earnings derived from investment of moneys on deposit in any debt service reserve fund, and any construction fund created with respect to any Contracts or Bonds to the extent such earnings are deposited in a debt service fund;

provided that, as to any such Bonds or installment payments due under any Contracts bearing or comprising interest at other than a fixed rate, the rate of interest used to calculate Debt Service shall be one hundred ten percent (110%) of the greater of:

(i) the then current variable interest rate borne by such Bonds or Contracts plus 2%, and

(ii) the highest variable rate borne over the preceding 12 months by outstanding variable rate debt issued by the District or, if no such variable rate debt is at the time outstanding, by variable rate debt of which the interest rate is computed by reference to an index comparable to that to be utilized in determining the interest rate for the debt then proposed to be issued;

provided further that if any series or issue of such Bonds or installment payments due under any Contracts have twenty-five percent (25%) or more of the aggregate principal amount of such series or issue due in any one year, Debt Service shall be determined for the Fiscal Year of determination as if the principal of and interest on such series or issue of such Bonds or installment payments were being paid from the date of incurrence thereof in substantially equal annual amounts over a period of thirty (30) years from the date of calculation; and

provided further that the amount on deposit in a debt service reserve fund on any date of calculation of Debt Service shall be deducted from the amount of principal due at the final maturity of the Bonds and Contracts for which such debt service reserve fund was established and in each preceding year until such amount is exhausted;

provided further that Debt Service shall be reduced by the amount of investment earnings credited to any debt service fund created with respect to Contracts or Bonds; and

provided further that if the Bonds or Contracts constitute Paired Obligations, the interest rate on such Bonds or Contracts shall be the resulting linked rate or the effective fixed interest rate to be paid by the District with respect to such paired obligations.

“Information Services” means the Electronic Municipal Market Access System of the Municipal Securities Rulemaking Board or such other services as are authorized by the Securities and Exchange Commission to receive notices of called bonds as the District may designate in a Written Request of the District delivered to the Trustee.

“Operation and Maintenance Expenses” means (i) costs spent or incurred for maintenance and operation of the Water System calculated in accordance with generally accepted accounting principles, including (among other things) the reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the District that are charged directly or apportioned to the Water System, including but not limited to salaries and wages of employees, payments to the Public Employees Retirement System, overhead, insurance, taxes (if any), fees of auditors, accountants, attorneys or engineers and insurance premiums, and including all other reasonable and necessary costs of the District or charges (other than debt service payments) required to be paid by it to comply with the terms of the Certificates or of this Agreement or any Contract or of any resolution or indenture authorizing the issuance of any Bonds or of such Bonds; and (ii) costs spent or incurred in the purchase of water for the Water System; but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature and all capital charges.

“Paired Obligations” means any Bond or Contract (or portion thereof) designated as Paired Obligations in the resolution, indenture or other document authorizing the issuance or

execution and delivery thereof, which are simultaneously issued or executed and delivered (i) the principal of which is of equal amount maturing and to be redeemed or prepaid (or cancelled after acquisition thereof) on the same dates and in the same amounts, and (ii) the interest rates which, taken together, result in an irrevocably fixed interest rate obligation of the District for the term of such Bond or Contract.

“Remarketing Agreement” means the Remarketing Agreement dated as of June 1, 1996, by and between the District and the Remarketing Agent as it may be amended from time to time.

“Termination Date” means the stated expiration date of the Facility as such date may be extended from time to time, or any earlier date on which the Facility then in effect shall terminate, expire or be cancelled.

“Trustee” means The Bank of New York Mellon Trust Company, as successor in interest to Chemical Trust Company of California, or any other bank or trust company which may at any time be substituted in its place pursuant to the terms of the Trust Agreement.

**Section 2. Amendment of Section 4.13.** Section 4.13 of the Original Installment Agreement is deleted in its entirety and amended to read as follows:

Section 4.13. Limitations on Parity Debt Obligations. The District may at any time execute any Contract or issue any Bonds, as the case may be, as Parity Debt, in accordance herewith, provided an Independent Financial Consultant or Certified Public Accountant shall render to and file with the District and the Trustee a written report certifying that Taxes and Net Revenues for any twelve (12) consecutive calendar months in the eighteen (18) calendar months immediately preceding the issuance of the Parity Debt adjusted as set forth below are at least equal to 125% of Debt Service, assuming such additional Contracts had been executed or additional Bonds had been issued at the beginning of such twelve-month period.

For purposes of calculating Net Revenues as set forth in the preceding paragraph, adjustments to the computations of Net Revenues may be made for the following:

(i) any change in service charges which has been adopted subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(ii) customers added to the Water System subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(iii) the estimated change in Net Revenues which will result from the connection of existing residences or businesses to the Water System within one year following completion of any project to be funded or system to be acquired from the proceeds of such additional Bonds or Contracts; and

(iv) the estimated change in Net Revenues which will result from services provided under any long-term, guaranteed contract that extends for the life of the

additional Bonds or Contracts if entered into subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts.

Notwithstanding the foregoing, Bonds issued or Contracts executed to refund Bonds or Contracts may be delivered without satisfying the conditions set forth above if Debt Service in each Fiscal Year after the Fiscal Year in which such Bonds are issued or Contracts executed is not greater than Debt Service would have been in each such Fiscal Year prior to the issuance of such Bonds or execution of such Contracts.

**Section 3. Amendment of Section 5.01.** Section 5.01(n) of the Original Installment Agreement is deleted in its entirety and Section 5.01(h) and (m) of the Original Installment Agreement are deleted in their entirety and amended to read as follows:

(h) The District will prepare and file with the Trustee and the Bank annually within one hundred eighty (180) days after the close of each Fiscal Year financial statements of the District for the preceding Fiscal Year prepared in accordance with generally accepted accounting principles, together with an Accountant's Report thereon.

(m) The District shall fix, prescribe, revise and collect rates, fees and charges for the services and commodities provided by the Water System which will be at least sufficient to yield during each Fiscal Year Taxes and Net Revenues equal to one hundred twenty-five percent (125%) of the Debt Service for such Fiscal Year. The District may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Taxes and Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of this section.

**Section 4. Nature of Amendment.** The District and the Corporation each hereby find and determine that this First Amendment is an amendment made in accordance with Section 12.04(a) of the Original Installment Purchase Agreement which has been consented to by the Remarketing Agent in its capacity as the owner of all outstanding Certificates on the Mandatory Tender Date and with the consent of the Bank.

**Section 5. Effect of Original Installment Sale Agreement.** Except as expressly set forth herein, all provisions of the Original Installment Sale Agreement remain in full force and effect.

**Section 6. Execution in Counterparts.** This First Amendment may be executed in several counterparts, each of which shall be deemed an original, and all of which shall constitute but one and the same instrument.

*[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK.]*

IN WITNESS WHEREOF, the parties hereto have executed this Installment Sale Agreement by their officers thereunto duly authorized as of the day and year first written above:

OTAY WATER DISTRICT

By: \_\_\_\_\_  
Its: General Manager

ATTEST:

\_\_\_\_\_  
Secretary of the Board of Directors

OTAY SERVICE CORPORATION

By: \_\_\_\_\_  
Its: Chief Financial Officer

ATTEST:

\_\_\_\_\_  
Secretary of the Board of Directors

ACKNOWLEDGED AND AGREED:

THE BANK OF NEW YORK MELLON TRUST  
COMPANY, N.A., as Trustee

By: \_\_\_\_\_  
Authorized Officer

CONSENTED TO BY:

UNION BANK, N.A.

By: \_\_\_\_\_  
Authorized Officer

**MPG DRAFT**  
**05/26/2011**

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**REIMBURSEMENT AGREEMENT**

dated as of June 1, 2011

between

**OTAY WATER DISTRICT**

and

**UNION BANK, N.A.**

relating to

**OTAY WATER DISTRICT**  
**\$15,400,000 Variable Rate Demand**  
**Certificates of Participation**  
**(1996 Capital Projects)**

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**REIMBURSEMENT AGREEMENT**, dated as of June \_\_, 2011, between **OTAY WATER DISTRICT**, a water district duly organized and existing under the Constitution and laws of the State of California (the “District”), and the **UNION BANK, N.A.**, a national banking association organized and existing under the laws of the United States (the “Bank”).

**RECITALS**

A. The District and the Otay Service Corporation, a nonprofit public benefit corporation duly organized and existing under the laws of the State of California (the “Corporation”) have entered into an Installment Sale Agreement, dated as of June 1, 1996 (as from time to time amended, the “Installment Sale Agreement”), whereby the Corporation agreed to sell to the District the Project (as defined herein), and the District agreed to purchase the Project from the Corporation.

B. Under the Installment Sale Agreement, the District is obligated to pay to the Corporation or its assigns Installment Payments and Additional Costs (as both terms are defined herein) for the purchase of the Project.

C. Pursuant to a Trust Agreement, dated as of June 1, 1996 (as from time to time amended or supplemented, the “Trust Agreement”), among the District, the Corporation and The Bank of New York Mellon Trust Company, N.A., as trustee (the “Trustee”), the successor to Chemical Trust Company of California, as original trustee, the District caused the execution and delivery of \$15,400,000 aggregate principal amount of Valuable Rate Demand Certificates of Participation (1996 Capital Projects) (the “Certificates”) of which \$\_\_\_\_\_ principal amount is currently outstanding.

D. The Corporation assigned the rights to receive the Installment Payments and Additional Costs, and the Corporation and the District granted a security interest in all

monies held by the Trustee under the Trust Agreement, to the Trustee for the benefit of the Owners of the Certificates and the Bank.

E. The District has requested the Bank to substitute and replace Landesbank Hessen-Thüringen Girozentrale, acting through its New York bank, as the original Letter of Credit issuer, and to issue its own irrevocable, transferable, direct draw letter of credit, in substantially the form of Exhibit A (such letter of credit and any successor letter of credit as provided in such letter of credit being the “Letter of Credit”), in the amount of up to \$\_\_\_\_\_ (the “Commitment”) of which \$\_\_\_\_\_ shall support the payment with respect to the remaining principal of the Certificates and \$\_\_\_\_\_ shall support the payment of up to \_\_\_\_\_ ( ) days’ accrued interest with respect to the Certificates computed at a rate of interest equal to twelve percent (12%) per annum.

## AGREEMENTS

**NOW, THEREFORE**, in consideration of the premises and in order to induce the Bank to issue the Letter of Credit, the parties hereto agree as follows:

### **ARTICLE I DEFINITIONS**

**SECTION 1.01**      Certain Defined Terms. As used in this Agreement, the following terms shall have the following meanings (such meanings to be equally applicable to both the singular and plural forms of the terms defined):

“Acquisition and Construction Costs” has the meaning assigned to that term in the Installment Sale Agreement.

“Additional Costs” has the meaning assigned to that term in the Installment Sale Agreement.

“Advance” means any Tender Advance. A drawing under the Letter of Credit that does not satisfy the conditions set forth in Section 3.03 does not constitute a Tender Advance and is payable on demand in accordance with Section 2.04.

“Available Amount” in effect at any time, means the maximum amount available to be drawn at such time under the Letter of Credit, the determination of such maximum amount to assume compliance with all conditions for drawing and no reduction for any amount drawn by an Interest Draft referred to in the Letter of Credit (unless such amount is not reinstated under the Letter of Credit).

“Bank Certificates” means any and all Certificates purchased by the Trustee by means of a Tender or Payment Draft, which Certificates are then, pursuant to the terms of the Trust Agreement, registered in the name of and owned by the Bank.

“Bankruptcy Code” means the Bankruptcy Code of the United States, Title 11 of the United States Code, as amended.

“Base Rate” means, for any day, the higher of (a) the sum of the Reference Rate plus 2.50% per annum or (b) the sum of the Federal Funds Rate plus 2.50% per annum or (c) 7.00% per annum.

“Bonds” has the meaning assigned to that term in the Installment Sale Agreement.

“Business Day” has the meaning assigned to that term in the Installment Sale Agreement.

“Certificates” has the meaning assigned to that term in Recital C.

“Claim” has the meaning assigned to that term in Section 7.14.

“Closing Date” means the date on which the Letter of Credit is issued.

“Code” means the Internal Revenue Code of the United States of America, Title 26 of the United States Code, as amended.

“Commitment” has the meaning assigned to that term in Recital E.

“Commitment Termination Date” has the meaning assigned to that term in Section 2.01.

“Contracts” has the meaning assigned to that term in the Installment Sale Agreement.

“Conversion Date” has the meaning assigned to that term in the Installment Sale Agreement.

“Corporation” has the meaning assigned to that term in Recital A.

“Custody Agreement” means the agreement dated as of June 1, 2011, by and between the Bank and Tender Agent, in the form of Exhibit B attached hereto.

“Debt” means (i) indebtedness for borrowed money or for the deferred purchase price of property or services, (ii) obligations as lessee under leases which are or should be, in accordance with generally accepted accounting principles, recorded as capital leases, and (iii) obligations under direct or indirect guaranties in respect of, and obligations (contingent or otherwise) to purchase or otherwise acquire, or otherwise to assure a creditor against loss in respect of, indebtedness or obligations of others of the kinds referred to in clause (i) or (ii) above.

“Default Rate” means a fluctuating interest rate equal to 3% per annum above the Base Rate in effect from time to time.

“Delivery Costs” has the meaning assigned to that term in the Installment Sale Agreement.

“Draw Date” has the meaning assigned to that term in Section 2.04.

“Draw Rate” means a fluctuating interest rate equal to the Base Rate in effect from time to time for 180 aggregate days and, thereafter, equal to 1% per annum above the Base Rate in effect from time to time.

“Event of Default” has the meaning assigned to that term in Section 6.01.

“Federal Funds Rate” means, for any day, the rate per annum (rounded upwards to the nearest 1/100 of 1%) equal to the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day; provided, that (a) if such day is not a Business Day, the Federal Funds Rate for such day shall be such rate on such transactions on the next preceding Business Day as so published on the next succeeding Business Day, and (b) if no such rate is so published on such next succeeding Business Day, the Federal Funds Rate for such day shall be the average rate charged the Bank on such day on such transactions.

“Final Draft” has the meaning assigned to that term in the Letter of Credit.

“Financial Statements” means, in the case of the District, its Statement of Financial Position as at a specific date, and the related Statement of Activities and Changes in Net Assets and of Cash Flows for the applicable period ended on such specific date.

“Fiscal Year” has the meaning assigned to that term in the Installment Sale Agreement.

“Fixed Rate” has the meaning assigned to that term in the Installment Sale Agreement.

“Fixed Rate Conversion Rate” has the meaning assigned to that term in the Installment Sale Agreement.

“Gross Revenues” has the meaning assigned to that term in the Installment Sale Agreement.

“Hazardous Substances” means (a) any oil, flammable substance, explosives, radioactive materials, hazardous wastes or substances, toxic wastes or substances or other wastes, materials or pollutants which (i) pose a hazard to the Project or to Persons on or about the Project or (ii) cause the Project to be in material violation of any applicable law; (b) asbestos in any form which is or could become friable, urea formaldehyde foam insulation, transformers or other equipment which contain dielectric fluid containing levels of polychlorinated biphenyls, or radon gas; (c) any chemical, material or substance defined as or included in the definition of “waste,” “hazardous substances,” “hazardous wastes,” “hazardous materials,” “extremely hazardous waste,” “restricted hazardous waste,” or “toxic substances” or words of similar import under applicable law including, but not limited to, the Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”), 42 USC §§9601 et seq.; the Resource Conservation and Recovery Act (“RCRA”), 42 USC §§9601 et seq.; the Hazardous Materials Transportation Act, 49 USC §§1801 et seq.; the Federal Water Pollution Control Act, 33 USC §§1251 et seq.; the California Hazardous Waste Control Law (“HWCL”), Cal. Health & Safety §§25100 et seq.; the Hazardous Substance Account Act (“HSAA”), Cal. Health & Safety §§25300 et seq.; the Underground Storage of Hazardous Substances Act, Cal. Health & Safety §§25280 et seq.; the Porter-Cologne Water Quality Control Act (the “Porter-Cologne Act”), Cal Water Code §§13000 et seq.; the Safe Drinking Water and Toxic Enforcement Act of 1986 (Proposition 65); and Title 22 of the California Code of Regulations, Division 4, Chapter 30; (d) any other chemical, material or substance, exposure to which is prohibited, limited or regulated by any governmental authority or agency or may or could pose a hazard to the health and safety

of the occupants of the Project or the owners and/or occupants of property adjacent to or surrounding the Project, or any other person coming into the Project or adjacent property; and (e) any other chemical, materials or substances which may or could pose a hazard to the environment.

“Independent Certified Public Accountant” has the meaning assigned to that term in the Installment Sale Agreement.

“Independent Financial Consultant” has the meaning assigned to that term in the Installment Sale Agreement.

“Interest Draft” has the meaning assigned to that term in the Letter of Credit.

“Installment Payments” has the meaning assigned to that term in the Installment Sale Agreement.

“Installment Payment date” has the meaning assigned to that term in the Installment Sale Agreement.

“Installment Sale Agreement” has the meaning assigned to that term in Recital A.

“Letter of Credit” has the meaning assigned to that term in Recital E and is sometimes referred to as the “Facility” in the Installment Sale Agreement.

“Margin Stock” means “margin stock” as such term is defined in Regulation T, U or X of the Federal Reserve Board.

“Maturity Date” means \_\_\_\_\_, 2014, or such later date as may have been agreed to by the District and the Bank pursuant to Section 2.08 hereof.

“Moody's” has the meaning assigned to that term in the Installment Sale Agreement.

“Net Proceeds” has the meaning assigned to that term in the Installment Sale Agreement.

“Official Statement” means the Official Statement dated June 17, 1996, relating to the Certificates, together with the documents incorporated therein by reference.

“Operation and Maintenance Expenses” has the meaning assigned to that term in the Installment Sale Agreement.

“Outstanding” has the meaning assigned to that term in the Installment Sale Agreement.

“Owner” or “Holder” or “Certificate Owner” or “Owner of a Certificate” or “Certificate Holder” or “Holder of a Certificate” has the meaning assigned to those terms in the Installment Sale Agreement.

“Parity Debt” has the meaning assigned to that term in the Installment Sale Agreement.

“Participant” means a banking or financial institution participating in the Letter of Credit and this Agreement pursuant to Section 7.13 hereof.

“Participation Agreement” means the document by which a Participant participates in the Letter of Credit and this Agreement, as provided in Section 7.13 hereof.

“Payment Draft” has the meaning assigned to that term in the Letter of Credit.

“Permitted Encumbrances” means, as of any particular time: (a) liens for general ad valorem taxes and assessments, if any, not then delinquent; (b) any right or claim of any mechanic, laborer, materialman, supplier or vendor filed or perfected in the manner prescribed by law after the Closing Date and which will be paid in the ordinary course of business or are being contested in good faith by the District; (c) easements, rights-of-way, mineral rights,

drilling rights and other rights, reservations, covenants, conditions or restrictions which exist of record as of the Closing Date; (f) easements, rights-of-way, mineral rights, drilling rights and other rights, reservations, covenants, conditions or restrictions which do not reduce the value of the Project and the improvements.

“Person” means any natural person, corporation, firm, association, partnership, government, governmental agency or any other entity, whether acting in an individual, fiduciary or other capacity.

“Priority Debt” has the meaning assigned to that term in the Installment Sale Agreement.

“Project” has the meaning assigned to that term in the Installment Sale Agreement.

“Rating Agency” means Moody's, S&P and any other rating agency which, at the time in question, shall be rating the Certificates, and their successors and assigns.

“Rebate Fund” has the meaning assigned to that term in the Installment Sale Agreement.

“Reference Rate” means the rate of interest publicly announced from time to time by the Bank as its “reference rate,” which is a rate set by the Bank based upon various factors including the Bank's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans, which may be priced at, above or below such announced rate.

“Related Documents” has the meaning assigned to that term in Section 2.12.

“Remarketing Agent” has the meaning assigned to that term in the Installment Sale Agreement.

“Remarketing Agreement” has the meaning assigned to that term in the Installment Sale Agreement.

“S&P” has the meaning assigned to that term in the Installment Sale Agreement.

“State” means the State of California.

“Stated Termination Date” has the meaning assigned to that term in the Letter of Credit.

“Substitute Facility” has the meaning assigned to that term in the Installment Sale Agreement.

“Taxes” has the meaning assigned to that term in the Installment Sale Agreement.

“Tender Advance” has the meaning assigned to that term in Section 2.05.

“Tender Agent” has the meaning assigned to that term in the Installment Sale Agreement and is sometimes referred to as the “Custody Agent” in the Installment Sale Agreement when acting in such capacity.

“Tender Draft” has the meaning assigned to that term in the Letter of Credit.

“Trust Agreement” has the meaning assigned to that term in Recital C.

“Trustee” has the meaning assigned to that term in Recital C.

“Water System” has the meaning assigned to that term in the Installment Sale Agreement.

**SECTION 1.02**      **Computation of Time Periods.** In this Agreement, in the computation of a period of time from a specified date to a later specified date, the word “from” means “from and including” and the words “to” and “until” each means “to but excluding.”

**SECTION 1.03**      **Accounting Terms.** All accounting terms not specifically defined herein shall be construed in accordance with generally accepted accounting principles

and practices consistent with those principles and practices promulgated or adopted by the Financial Accounting Standards Board and the Board of the American Institute of Certified Public Accountants, their respective predecessors and successors.

**SECTION 1.04**      **References to Other Documents.** All terms defined herein by reference to another document shall have the meanings ascribed to such terms in such other documents existing as of the date hereof without regard to subsequent modification or amendment unless the Bank shall have consented otherwise in writing.

**ARTICLE II**  
**AMOUNT AND TERMS OF THE LETTER OF CREDIT**

**SECTION 2.01**      **The Letter of Credit.** The Bank shall, under the terms and conditions hereinafter set forth, issue the Letter of Credit to the Trustee at any time during the period from the date hereof to and including July 29, 2011 (the “Commitment Termination Date”) in the aggregate amount of the Commitment and expiring on the Maturity Date unless sooner terminated pursuant to the terms hereof.

**SECTION 2.02**      **Issuing the Letter of Credit.** The Letter of Credit shall be issued on at least five Business Days' notice from the District to the Bank specifying the date thereof. On the date specified by the District in such notice and upon fulfillment of the applicable conditions set forth in Article III, the Bank will issue the Letter of Credit to the Trustee. Payments made under the Letter of Credit by the Bank will be made from its own funds.

**SECTION 2.03**      **Commissions.**

(a)      **Closing Fee:** The District shall pay, or cause to be paid, to the Bank, on the Closing Date, a closing fee equal to \$5,000.00

(b) Facility Fee: The District shall pay, or cause to be paid, to the Bank a facility fee based on the Available Amount in effect, from the date of issuance of the Letter of Credit until the Stated Termination Date, at a rate of 1.10% per annum. The facility fee shall be payable in advance, upon the issuance of the Letter of Credit and upon each anniversary of such issuance. Once paid, the facility fee shall be deemed earned and shall not be refundable.

(c) Early Termination Fee: If the Letter of Credit shall be terminated or permanently reduced prior to the second anniversary of the Closing Date for any reason, the District shall pay, or cause to be paid, to the Bank, at the time of termination or permanent reduction, an early termination fee based on the original amount of the Commitment for the period from the date the Letter of Credit was issued to the second anniversary of the Closing Date, at the rate of 1.10% per annum, less the amount of any facility fees already paid. There shall be no early termination fee required to be paid to the Bank for any termination of the Letter of Credit occurring as the result of a downgrade of the Bank's short-term credit ratings to below P-1/A-1/F1.

(d) Transfer Fee: The District shall pay, or cause to be paid, to the Bank, upon each transfer of the Letter of Credit in accordance with its terms, a transfer commission equal to \$2,000. A transfer is deemed to have occurred whenever the Trustee is replaced, substituted or changed as a result of sale, assignment, merger, consolidation, reorganization or an act of law.

(e) Draw Fee: The District shall pay, or cause to be paid, to the Bank upon each draw under the Letter of Credit a sum equal to \$250, payable on the Draw Date.

(f) Default Fee: The District shall pay, or cause to be paid, to the Bank during the period of any Event of Default hereunder, regardless of whether the Bank has exercised any of its remedies as described in Section 6.02 below, a default fee based on the Available Amount in effect, from the date such Event of Default has occurred until the earlier of the date such Event of Default is cured or the Stated Termination Date, at the rate of 3.00% per annum. The default fee shall be payable monthly in arrears, on the last day of each month, and on the day the Event of Default is cured or, if earlier, the Stated Termination Date.

(g) Cancellation Fee: If the Letter of Credit shall not be issued by July 29, 2011, for any reason, the District shall pay to the Bank, on such date, a cancellation fee of \$50,000.

**SECTION 2.04** Reimbursement On Demand. Subject to the provisions of Sections 2.05 and 2.06, the District shall pay or cause the Trustee to pay to the Bank on each date on which the Bank shall pay any amount under the Letter of Credit pursuant to any Payment Draft (the "Draw Date"), (i) a sum equal to the amount so paid, plus (ii) interest on the unreimbursed amount from the Draw Date until reimbursement is received by the Bank in full. Such interest shall be at the Default Rate in effect from time to time.

**SECTION 2.05** Tender Advances. In the event the Bank makes any payment under the Letter of Credit pursuant to a Tender Draft and the conditions set forth in Section 3.03 have been fulfilled, such payment shall constitute an Advance made by the Bank to the District on the date and in the amount of such payment, each such Advance being a "Tender Advance" and collectively the "Tender Advances." The unpaid principal amount of any Tender Advance and all accrued and unpaid interest thereon shall be repaid in accordance with the terms of Sections 2.06 and 2.07. Upon payment under the Letter of Credit pursuant to a Tender Draft,

the Certificates so purchased shall become Bank Certificates and shall be owned by the Bank but held by the Tender Agent pursuant to the terms of the Custody Agreement. The Bank shall be entitled to all rights and remedies of a Certificate Owner so long as any Bank Certificates remain outstanding.

**SECTION 2.06**      **Interest on Tender Advances.** The District shall pay or caused to be paid interest on the unpaid principal amount of each Tender Advance from the date of such Advance until such principal amount of such Tender Advance becomes due, payable monthly on the last Business Day of each calendar month with respect to the month then ended, at a fluctuating rate of interest per annum equal to the Draw Rate in effect from time to time; provided, however, that in the event such interest is not paid on any outstanding Tender Advance when due and payable, the District shall pay interest on the principal amount of such Tender Advance and the amount of the unpaid interest, if any, on demand, at the Default Rate in effect from time to time, beginning from the date the unpaid interest first started to accrue, which payment by the District shall be deemed, as of the date hereof, to be a contractual contingent liability of the District within the Fiscal Year in which the obligation was incurred; provided further, that any interest paid by the City with respect to Bank Certificates while Bank Certificates shall be taken into account for purposes of calculating the amounts due and payable pursuant to this Section 2.06.

**SECTION 2.07**      **Prepayments; Reinstatement of Letter of Credit Amounts.**

(a)      The District may on any Business Day, upon at least two Business Days' notice to the Bank, prepay the outstanding amount of any Tender Advance, in whole or in part, with accrued interest to the date of such prepayment on the amount prepaid. Such payments

when accompanied by a certificate completed and signed by the Trustee (with a copy to the District) in substantially the form of Annex D to the form of Letter of Credit shall be applied by the Bank in reimbursement of such drawings (and as prepayment of Tender Advances resulting from such drawings in the manner described above); and the District irrevocably authorizes the Bank to rely on such certificate and to reinstate the Letter of Credit in accordance therewith.

(b) Prior to or simultaneously with the remarketing of Bank Certificates acquired by the Tender Agent with the proceeds of one or more Tender Advances, the District shall cause the Trustee on behalf of the District to repay such Tender Advances (in the order in which they were made) by paying to the Bank an amount equal to the sum of (i) the aggregate principal amount of the Bank Certificates being remarketed or to be remarketed plus (ii) that aggregate amount of accrued and unpaid interest on such principal amount which was paid by a drawing or drawings under such Tender Draft or Drafts; provided further, that any interest paid by the District with respect to Bank Certificates while Bank Certificates shall be taken into account for purposes of calculating the amounts due and payable pursuant to this Section 2.07(b). Such payments when accompanied by a certificate completed and signed by the Trustee in substantially the form of Annex D to the form of Letter of Credit shall be applied by the Bank in reimbursement of such drawings (and as prepayment of Tender Advances resulting from such drawings in the manner described above); and the District irrevocably authorizes the Bank to rely on such certificate and to reinstate the Letter of Credit in accordance therewith.

(c) If any change in any law or regulation or in the interpretation thereof by any court or administrative or governmental authority charged with the administration thereof shall either (i) impose, modify or deem applicable any reserve, special deposit or similar requirement against letters of credit issued by, or assets held by, or deposits in or for the account

of, the Bank or (ii) impose on the Bank any other condition regarding this Agreement, the Letter of Credit, or the Advances, and the result of any event referred to in clause (i) or (ii) above shall be (A) to increase the cost to the Bank of issuing or maintaining the Letter of Credit or making or maintaining any Advance or holding any Bank Certificates or (B) reduce the amount receivable or to be received with respect to the Letter of Credit or any Advance (which increase in cost or reduction in amount shall be determined by the Bank's reasonable allocation of the aggregate of such cost increases or such reduced amounts resulting from such event), then, within 15 days after a written demand by the Bank, the District shall pay to the Bank, from time to time as specified by the Bank, additional amounts which shall be sufficient to compensate the Bank for such increased cost or such reduced amount. A certificate setting forth such increased cost incurred by the Bank as a result of any event mentioned in clause (i) or (ii) above and giving a reasonable explanation thereof, submitted by the Bank to the District, shall constitute such demand and shall, in the absence of manifest error, be conclusive and binding for all purposes as to the amount thereof.

(d) In the event that the Bank shall have determined that the adoption after the date hereof of any law, rule or regulation regarding capital adequacy, or any change therein or in the interpretation or application thereof or compliance with any request or directive regarding capital adequacy (whether or not having the force of law) from any central bank or governmental authority, does or shall have the effect of reducing the rate of return on the Bank's capital as a consequence of its obligations hereunder to a level below that which the Bank could have achieved but for such adoption, change or compliance (taking into consideration the Bank's policies with respect to capital adequacy) by any amount deemed by the Bank to be material, then from time to time, within 15 days after demand by the Bank, the District shall pay to the

Bank such additional amount or amounts as will compensate the Bank for such reduction, and the Bank shall provide the District with a statement in reasonable detail setting forth the calculation of the amount of such compensation. Such statement shall constitute demand for payment of the amount or amounts set forth therein and shall, in the absence of manifest error, be conclusive and binding for all purposes as to the amount or amounts thereof.

**SECTION 2.08      Requests for Extension of Maturity Date.** At least 60 but not more than 90 days before the second anniversary of the Closing Date, and at least 60 but not more than 90 days before each subsequent anniversary of the Closing Date, if any, the District may request the Bank in writing to extend the Maturity Date for a period of at least one year. If the District shall make such a request, the Bank shall, within 30 days of receipt of such request from the District, notify the District in writing whether or not the Bank consents to such request and, if the Bank does so consent, the conditions of such consent. If the Bank shall not so notify the District, the Bank shall be deemed not to have consented to such request. The District and the Bank agree, and the District understands, that the granting of each such request is completely at the discretion of the Bank, and that the granting of any one or more of such requests does not obligate the Bank to grant any subsequent such request. If the Bank determines to grant any such request, the Maturity Date shall be extended for the applicable period.

**SECTION 2.09      Payments and Computations.** The District shall make, or cause to be made, each payment hereunder not later than 1:00 P.M. (Pacific time) on the day when due without deduction or offset in lawful money of the United States of America to the Bank at its address referred to in Section 7.03 in same-day funds or in accordance with the wire instructions in such Section. Computations of the Draw Rate, Default Rate, facility fee, default

fee, termination fee and all other commissions and fees established herein (as applicable) shall be made by the Bank on the basis of a year of 360 days for the actual number of days elapsed.

**SECTION 2.10**      **Non-Business Days.** Whenever any payment to be made hereunder shall be stated to be due on a day which is not a Business Day, such payment shall be made on the next succeeding Business Day, and such extension of time shall in such case be included in the computation of payment of interest or commission, as the case may be.

**SECTION 2.11**      **Evidence of Advances.** The Bank shall maintain in accordance with its usual practice an account or accounts evidencing the indebtedness of the District resulting from each drawing under the Letter of Credit and from each Advance made from time to time hereunder and the amounts of principal and interest payable and paid from time to time hereunder. In any legal action or proceeding in respect of this Agreement, the entries made in such account or accounts shall be conclusive evidence of the existence and amounts of the obligations of the District therein recorded; provided, however, that any failure to make entries or any error in doing so shall not limit or otherwise affect the obligations of the District under this Agreement.

**SECTION 2.12**      **Obligations Absolute.** The payment obligations of the District under this Agreement shall be unconditional and irrevocable, and shall be paid strictly in accordance with the terms of this Agreement under all circumstances, including, without limitation, the following circumstances:

(i) any lack of validity or enforceability of the Letter of Credit, the Certificates, the Trust Agreement, the Installment Sale Agreement, the Custody Agreement, the Remarketing Agreement, or any other agreement or instrument relating thereto (collectively the "Related Documents");

(ii) any amendment or waiver of, or any consent to departure from, all or any of the terms of the Related Documents;

(iii) the existence of any claim, set-off, defense or other right which the District may have at any time against the Trustee or any other beneficiary, or any transferee, of the Letter of Credit (or any persons or entities for whom the Trustee, any such beneficiary or any such transferee may be acting), the Bank, or any other person or entity, whether in connection with this Agreement, the transactions contemplated by this Agreement or the Related Documents, or any unrelated transaction;

(iv) any statement or any other document presented by or on behalf of the Trustee under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect;

(v) payment by the Bank under the Letter of Credit against presentation of a draft or certificate which does not comply with the terms of the Letter of Credit;  
or

(vi) any non-application or misappropriation by the Trustee, the Paying Agent or the Tender Agent or otherwise of the proceeds of any drawing or Advance; or

(vii) the failure by the Bank to honor any drawing under the Letter of Credit or to make any payment demanded under the Letter of Credit on the grounds that the demand for such payment does not conform to the terms and conditions of the Letter of Credit; or

(viii) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

**SECTION 2.13      Security for Draws.** To provide for the performance of

the District hereunder and the payment of all amounts due or to become due to the Bank, (i) the District has caused the Corporation to transfer, assign and set over to the Trustee, for the benefit of the Owners of the Certificates and the Bank, all of the Corporation's rights under the Installment Sale Agreement, subject to certain exceptions as set forth therein and (ii) both the District and the Corporation have granted to the Trustee and the Bank, pursuant to the terms of the Trust Agreement, a lien on and security interest in all monies in the funds held by the Trustee, including Installment Payments and Additional Costs on deposit therein, other than monies held in the Rebate Fund.

**ARTICLE III  
CONDITIONS PRECEDENT**

**SECTION 3.01      Condition Precedent to Issuance of the Letter of Credit.**

The obligation of the Bank to issue the Letter of Credit is subject to the condition precedent that the Bank shall have received on or before the date of the issuance of the Letter of Credit the following, each appropriately dated, in form, number and substance satisfactory to the Bank:

(a) A transcript containing copies of all documentation required at the time the Certificates were issued or relating to the Certificates and the Trust Agreement, including but not limited to all opinions issued in connection therewith.

(b) Originals (or copies certified to be true copies by an appropriate official of the District) of all governmental and regulatory approvals necessary for the District to have issued the Certificates and to enter into this Agreement and the Related Documents to which it is a party and to perform its obligations as contemplated hereby and thereby, and of all other documents evidencing any other necessary District action.

(c) To the extent not included in (a) above, copies of the resolutions of the District authorizing the execution, delivery and performance of this Agreement and the Related Documents to which it is a party, certified by an appropriate official of the District (which certification shall include a statement to the effect that such resolutions are in full force and effect on the date of the issuance of the Letter of Credit).

(d) A certificate of the District certifying the names and true signatures of the officials of the District authorized to sign this Agreement and the Related Documents to which it is a party and the other documents to be delivered by the District hereunder.

(e) Originals (or copies certified to be true copies by an appropriate official of the Corporation) of all governmental and regulatory approvals necessary for the Corporation to have entered into or enter into the Related Documents to which it is a party and to perform its obligations as contemplated thereby, and of all other documents evidencing any other necessary Corporation action.

(f) To the extent not included in (d) above, copies of the resolutions of the Corporation authorizing the execution, delivery and performance of the Related Documents to which it is a party, certified by an appropriate official of the Corporation (which certification shall include a statement to the effect that such resolutions are in full force and effect on the date of the issuance of the Letter of Credit).

(g) A certificate of the Corporation certifying the names and true signatures of the officials of the Corporation authorized to sign the Related Documents to which it is a party and the other documents to be delivered by the Corporation hereunder.

(h) A certificate of the Trustee certifying the names and true signatures of the officials of the Trustee authorized to sign the Related Documents to which it is a party and the other documents to be delivered by the Trustee hereunder.

(i) A certificate of the Tender Agent certifying the names and true signatures of the officials of the Tender Agent authorized to sign the Related Documents to which it is a party, including but not limited to the Custody Agreement, and the other documents to be delivered by the Tender Agent hereunder.

(j) An opinion of \_\_\_\_\_, special counsel to the District, in substantially the form of Exhibit C hereto and as to such other matters as the Bank may reasonably request, including the right to rely on its opinion as rendered at the time the Certificates were originally issued.

(k) An opinion of \_\_\_\_\_, special counsel to the Corporation, entitling the Bank to rely on its opinion as rendered at the time the Certificates were originally issued.

(l) An opinion of \_\_\_\_\_, bond counsel, entitling the Bank to rely on its opinion as rendered at the time the Certificates were originally issued.

(m) An executed copy of the Trust Agreement.

(n) An executed copy of the Custody Agreement.

(o) An executed copy of this Agreement.

(p) An executed copy of the Installment Sale Agreement.

(q) A copy of the CLTA leasehold title policy to be obtained by the District, showing the District as the beneficial owner under the Installment Sale Agreement, evidencing no exceptions to title other than the Permitted Encumbrances.

(r) Copies of the policies of insurance required to be obtained by the District under the Installment Sale Agreement along with the certifications thereof required pursuant to the Installment Sale Agreement and any applicable approvals of the Bank required under Section 5.01 hereof.

(s) A certificate from the Trustee as to the authentication and delivery of the Certificates.

(t) Executed copies of all other Related Documents.

**SECTION 3.02 Additional Conditions Precedent to Issuance of the**

**Letter of Credit.** The obligation of the Bank to issue the Letter of Credit shall be subject to the further conditions precedent that on the date of the issuance of the Letter of Credit:

(a) the following statements shall be true and the Bank shall have received a certificate signed by a duly authorized official of the District, dated the date of such issuance, stating that:

(i) The representations and warranties contained in Section 4.01 of this Agreement are correct on and as of the date of issuance of the Letter of Credit as though made on and as of such date; and

(ii) No event has occurred and is continuing, or would result from the issuance of the Letter of Credit, which constitutes an Event of Default or would constitute an Event of Default but for the requirement that notice be given or time elapse or both;

(b) the Bank shall have received such other approvals, opinions or documents as the Bank may reasonably request; and

(c) the District shall have paid or reimbursed the Bank for its costs and expenses as provided in Section 7.09.

**SECTION 3.03      Conditions Precedent to Each Advance.** Each payment made by the Bank under the Letter of Credit pursuant to a Tender Draft shall constitute an Advance hereunder (i.e., a drawing not payable on demand) only if on the date of such payment no event has occurred and is continuing, or would result from such payment, which constitutes an Event of Default or would constitute an Event of Default but for the requirement that notice be given or time elapse or both. Unless the District shall have previously advised the Bank in writing that the above statement is no longer true, the District shall be deemed to have represented and warranted, on the date of each payment by the Bank under the Letter of Credit pursuant to a Tender Draft that on the date of such payment the above statement is true. Upon expiration or sooner termination of the Letter of Credit, any Tender Advances outstanding shall be repayable by District in accordance with Section 2.05.

**ARTICLE IV  
REPRESENTATIONS AND WARRANTIES**

**SECTION 4.01      Representations and Warranties of the District.** The District represents and warrants as follows:

(a) The District is a municipal water district duly organized and existing under and by virtue of the Constitution and laws of the State of California and is possessed of full powers to lease and purchase real and personal property and to enter into contracts such as this Agreement and each of the Related Documents to which it is a party, which powers have been validly exercised in connection with the transactions effected by this Agreement and the Related Documents.

(b) The execution, delivery and performance by the District of this Agreement and the Related Documents to which it is a party are within the District's powers, have been duly authorized by all necessary governmental action, and do not and will not contravene or constitute a default under any provision of applicable law or regulation or of any law, determination, award, regulation, judgment, injunction, order, decree, rule or writ applicable to the District, or any indenture, lease, instrument, agreement or other contractual restriction binding on the District or its property, and do not and will not result in or require the creation or imposition of any lien, security interest or other charge or encumbrance upon or with respect to any of its properties, except as contemplated by such Related Documents; the District is not in violation of or in default under any law, order, rule, regulation, writ, judgment, injunction, decree, determination or award or any indenture, agreement, lease, instrument or other contractual restriction binding on or affecting the District which violation or default would adversely impair the ability of the District to perform its obligations hereunder or under the Related Documents to which it is a party.

(c) All authorizations, approvals, legally required orders, consents and other action by, and notice to or filing or registration with, any governmental authority, regulatory body or other public boards or bodies have been obtained or will be obtained for the

due execution, delivery and performance by the District of this Agreement and the Related Documents to which it is a party, and all of the transactions contemplated thereby.

(d) This Agreement has been duly authorized, executed and delivered by the District and, assuming the due authorization, execution and delivery by the other parties thereto, constitutes the legal, valid and binding obligation of the District, enforceable against the District in accordance with its terms. Each of the Related Documents to which the District is a party has been duly authorized, executed and delivered by the District and, assuming the due authorization, execution and delivery by the other parties thereto, constitutes the legal, valid and binding obligation of the District, enforceable against the District in accordance with its terms.

(e) The annual audited Financial Statements of the District for the 20\_\_ - 20\_\_ Fiscal Year, approved by the governing board of the District, fairly present, in conformity with the procedures set forth in \_\_\_\_\_, as the same may from time to time be amended, the financial position of the District as of the date thereof and the results of operations and changes in financial position for the periods indicated and the budget of the District for the 20\_\_-20\_\_ Fiscal Year delivered to the Bank is the budget adopted by the governing board of the District for that Fiscal Year. Since the date of the most recent Financial Statements there has been no material adverse change in the condition or operations of the District not disclosed in such information and no event has occurred which materially adversely affects the ability of the District to perform its obligations under this Agreement or any of the Related Documents to which it is a party.

(f) There are no actions, suits or proceedings, and no proceedings before any governmental commission, board, bureau or other administrative agency, pending, or,

to the knowledge of the District, threatened against or affecting the District which will (to the extent not covered by insurance) in the opinion of the District have a material adverse effect on the business, financial condition or results of operations of the District or which in any manner questions the validity of this Agreement or any of the Related Documents.

(g) The proceeds of the Certificates were expended on the Project which serves essential governmental functions and public purposes of the District.

(h) The District makes the representations and warranties made by it in the Related Documents to and for the benefit of the Bank as if the same were set forth at length in this Agreement.

(i) To the best knowledge of the District, there is no amendment, or proposed amendment certified for placement on a statewide ballot, to the Constitution of the State or any published administrative interpretation of the Constitution of the State or any State law, or any legislation which has passed either house of the State legislature or is under consideration by any conference or similar committee, or any published judicial decision interpreting any of the foregoing, the effect of which is to materially adversely affect the ability of the District to perform its obligations under this Agreement or any of the Related Documents to which it is a party.

(j) The Trust Agreement creates a valid security interest in the funds and accounts created under the Trust Agreement and the moneys, including, without limitation, the Installment Payments and Additional Costs on deposit therein, as security for the punctual payment of the interest and principal due with respect to the Certificates and the amounts owing to the Bank. All action necessary to create a first and exclusive lien on such funds and accounts

and on moneys on deposit therein, including the Installment Payments and Additional Costs, has been duly and validly taken.

(k) The Corporation has transferred, assigned and set over to the Trustee, for the benefit of the Owners of the Certificates and the Bank, all of the Corporation's rights under the Installment Sale Agreement, except as set forth therein. All action necessary to transfer, assign and set over such rights in the Installment Sale Agreement has been duly and validly taken.

(l) The Official Statement is, and any supplement or amendment to either shall be, accurate in all material respects for the purpose for which its use is, was or shall be, authorized; and the Official Statement does not, and any such supplement or amendment will not, contain any untrue statement of a material fact or omit to state any material fact necessary to make the statements made therein, in the light of the circumstances under which they are or were made, not misleading.

(m) After due investigation, there is not constructed, stored, deposited, disposed, placed or located on or in the Project any Hazardous Substances except such Hazardous Substances as may be incident to office uses and uses, all in accordance with applicable laws. The District has not stored or caused to be stored upon the Project any Hazardous Substances nor, after due investigation and inquiry, have any of District's predecessors in interest stored or caused to be stored any Hazardous Substances on or in the Project.

(n) The District does not enjoy any rights of immunity on the grounds of sovereign immunity in respect of its obligations under this Agreement or any Related Documents.

(o) The District has not been notified of any listing or proposed listing by the Internal Revenue Service to the effect that the District is an issuer of obligations whose arbitrage certifications may not be relied upon.

(p) The District has not taken any action or omitted to take any action, and knows of no action taken or omitted to be taken by any other Person, which action, if taken or omitted, would adversely affect the exclusion of interest on the Certificates from gross income for Federal income tax purposes or the exemption of such interest from State of California personal income taxes.

(q) The District is not engaged in the business of extending credit for the purpose of purchasing or carrying Margin Stock, and no proceeds of any Certificates will be used to extend credit to others for the purpose of purchasing or carrying any Margin Stock.

## ARTICLE V COVENANTS OF THE DISTRICT

**SECTION 5.01**     **Affirmative Covenants.** So long as a drawing is available under the Letter of Credit or the Bank shall have any Commitment hereunder or the District shall have any obligation to pay any amount to the Bank hereunder, the District will, unless the Bank shall otherwise consent in writing:

(a)     **Maintenance of Insurance.** Maintain insurance with responsible and reputable insurance companies or associations in such amounts and covering such risks as is

usually carried by water districts engaged in similar businesses and owning similar properties in the same general areas in which the District operates; provided, however, in the event the District elects to purchase insurance which has, as part of its terms, deductibles, the District must first obtain the Bank's approval as to amount and method of funding of such deductibles. The District also agrees that in the event of any failure to comply with such insurance requirements as contained herein, the Bank may purchase such insurance as it shall deem satisfactory, and all premiums, fees, costs, charges and expenses related thereto shall be paid by the District to the Bank upon demand.

(b) Preservation of Existence, Etc. Preserve and maintain its existence, rights (statutory), and franchises as a water district duly organized and existing under the Constitution and laws of the State.

(c) Compliance with Laws, Etc. Comply with the requirements of all applicable laws, rules, regulations and orders of any governmental authority, the non-compliance with which would materially adversely affect its ability to make Installment Payments or Additional Costs as required under the Installment Sale Agreement.

(d) Visitation Rights. At any reasonable time and from time to time, permit the Bank or any agents or representatives thereof to examine and make copies of and abstracts from the records' and books of account of the District and to discuss the affairs, finances and accounts of the District.

(e) Keeping of Books. Keep proper books of record and account, in which full and correct entries shall be made of all financial transactions and the assets and

business of the District, in accordance with generally accepted accounting principles consistently applied.

(f) Maintenance of Properties Etc. Maintain and preserve all of its properties which are used or useful in the conduct of the Project in good working order and condition, making all repairs or replacements as necessary, including but not limited to repairs or replacements necessitated by the occurrence of fire, flood, earthquake or any other event causing damage to the Project.

(g) Performance and Compliance with Other Covenants. Perform and comply with each of the terms, covenants and conditions set forth in this Agreement and the Related Documents to which the District is a party.

(h) Reporting Requirements. Furnish to the Bank the following:

(i) as soon as available, and in any event on or before December 31 of each year of the District, the District's audited Financial Statements accompanied by a certificate of a duly authorized officer of the District stating that as of the date of the audited Financial Statements there exists no Event of Default and no event which, with the passage of time or giving of notice, would constitute an Event of Default;

(ii) within 60 days of the final adoption of the annual budget of the District, but in no event later than September 1 of each year, a copy of the District's adopted budget;

(iii) as soon as possible, and in any event within five (5) days after the occurrence of each Event of Default or each event which, with the giving of notice or lapse of time, or both, would constitute an Event of Default, continuing on the date of such

statement, a statement of the chief financial officer of the District setting forth details of such Event of Default or event and the action which the District proposes to take with respect thereto;

(iv) at the time the budget is furnished to the Bank pursuant to clause (ii) above, but in no event later than September 1 of each year, (a) a certificate signed by the District certifying that the District has made the appropriations required in Section 5.01(l), (b) a copy of the current investment policy of the District for monies held in all funds and accounts of the District, and (c) a detailed description of the District's investment portfolio;

(v) within fifteen (15) days of incurring or issuing any obligations, including but not limited to loans, bonds and agreements with regard to certificates of participation, payable in whole or in part from the general fund of the District, a copy of any official statement, private placement or offering memorandum prepared in connection with such obligations;

(vi) promptly after the commencement thereof, notice of all actions, suits and proceedings before any court or governmental department, commission, board, bureau, agency or instrumentality, domestic or foreign, which materially affect the ability of the District to pay Installment Payments or Additional Costs under the terms of the Installment Sale Agreement; and

(vii) promptly, upon knowledge thereof, notice of (a) any and all claims of Hazardous Substances made against the District or the Project; (b) any remedial action taken by the District in response to any Hazardous Substances on, under or about the Project; (c) the District's discovery of any occurrence or condition on the real property adjoining or in the vicinity of the Project that could cause the Project or any part thereof to be classified as "border-zone property" under the provisions of California Health and Safety Code Sections 25220 et seq.

or any regulation adopted in accordance therewith or to be otherwise subject to any restrictions on the ownership, occupancy, transferability or use of the Project under any laws regulation or pertaining to Hazardous Substances; and

(viii) such other information respecting the business, properties or the condition or operations, financial or otherwise, of the District or the Project as the Bank may from time to time reasonably request.

(ix) at the time the budget is furnished to the Bank pursuant to clause (ii) above, but in no event later than September 1 of each year, a certificate signed by the District describing the insurance carried by the District with regard to the Project, including the name of the provider, the type of insurance, the amount of the coverage, the expiration date of the policy if any, and the amount of the deductibles, if any;

(x) at the time renewal takes place, evidence of renewal of each policy of insurance described in the certificate furnished pursuant to clause (ix) above;

All dates referred to above assume that the District will maintain its Fiscal Year end on June 30. If the Fiscal Year is changed, the dates referred to above will be changed accordingly.

(i) Return of Letter of Credit. Upon the occurrence of the Stated Termination Date, cause the Trustee to surrender the Letter of Credit to the Bank for cancellation.

(j) Emergency Loans. Use its best efforts to seek any additional sources which are available to it, including existing and any future federal, state or local loan or funding programs, in order to cure any Event of Default hereunder; to reimburse, in full, the Bank for any drawings under the Letter of Credit, whether designated as “Advances” or

otherwise; and to pay, in full, any other amounts owing by the District to the Bank under the terms of this Agreement.

(k) Annual Appropriations. Make annual appropriations at levels to make Installment Payments as required under the Installment Sale Agreement and to pay all obligations of the District owing to the Bank hereunder.

(l) Additional Sources. Use its best efforts to seek and utilize additional sources of funds legally available to it in order to reimburse the Bank, in full, for drawings under the Letter of Credit and other amounts owing hereunder.

(m) Net Proceeds. Use Net Proceeds for the reconstruction and rehabilitation of the Project or, if the Net Proceeds are insufficient for such purpose or the District elects to do so, use Net Proceeds to redeem Certificates then Outstanding.

(n) Water System Rates, Fees and Charges. Fix, prescribe, revise and collect rates, fees and charges for the services and commodities provided by the Water System which will be at least sufficient to yield during each Fiscal Year Taxes and Net Revenues equal to one hundred twenty-five percent (125%) of the Debt Service for such Fiscal Year. The District may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Taxes and Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of this Section.

**SECTION 5.02** **Negative Covenants.** So long as a drawing is available under the Letter of Credit or the Bank shall have any Commitment hereunder or the District shall

have any obligation to pay any amount to the Bank hereunder, the District will not, without the written consent of the Bank:

(a) Amendment of Any Related Document. Enter into or consent to any amendment or modification of the Trust Agreement, Installment Sale Agreement or any other Related Document.

(b) Encumbrances. Create any encumbrance which either directly or indirectly creates a lien or an adverse effect on the assets and revenues on which the Bank or the Owners of the Certificates have a lien pursuant to this Agreement or the Trust Agreement.

(c) Ranking Obligations. Take any action or actions which would result in the District's obligations to the Trustee and the Bank hereunder not ranking at least pari passu in right of payment with all unsecured obligations of the District to the other creditors.

(d) Debt Limitation. Create, incur, assume or otherwise become or remain obligated in respect of, or permit to be outstanding, or suffer to exist, any Debt other than Parity Debt except, with respect to any issuance of Parity Debt proposed by the District, an Independent Financial Consultant or Certified Public Accountant shall first render to and file with the District and the Trustee a written report certifying that Taxes and Net Revenues for any twelve (12) consecutive calendar months in the eighteen (18) calendar months immediately preceding the issuance of the Parity Debt adjusted as set forth below are at least equal to 125% of Debt Service, assuming such additional Contracts had been executed or additional Bonds had been issued at the beginning of such twelve-month period.

For purposes of calculating Net Revenues as set forth in the preceding paragraph, adjustments to the computations of Net Revenues may be made for the following:

(i) any change in service charges which has been adopted subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(ii) customers added to the Water System subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(iii) the estimated change in Net Revenues which will result from the connection of existing residences or businesses to the Water System within one year following completion of any project to be funded or system to be acquired from the proceeds of such additional Bonds or Contracts; and

(iv) the estimated change in Net Revenues which will result from services provided under any long-term, guaranteed contract that extends for the life of the additional Bonds or Contracts if entered into subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts.

Notwithstanding the foregoing, Bonds issues or Contracts executed to refund Bonds or Contracts may be delivered without satisfying the conditions set forth above if Debt Service in each Fiscal Year after the Fiscal Year in which such Bonds are issued or Contracts executed is not greater than Debt Service would have been in each such Fiscal Year prior to the issuance of such Bonds or execution of such Contracts.

(e) Investment Limitations. Directly or indirectly, through mutual or pooled funds or otherwise, invest in instruments whose yield reacts inversely to the market, including but not limited to so-called inverse floaters, or invest in reverse repurchase agreements unless with respect to such reverse repurchase agreements (i) the term of the contract relating

thereto is for a period of no more than 120 days and (ii) the monies obtained from investing in a reverse repurchase agreement is reinvested for a period no longer than the maturity of the reverse repurchase agreement from which such monies were obtained.

(f) Leverage Restrictions. Permit or allow its investment portfolio, or the portfolio of any funds or pooled funds in which it invests, to be leveraged by more than 25%.

(g) Liquidity. Encumber its cash position nor schedule the interest payment dates and maturities of its investments in a manner which impedes, hinders or interferes with the availability of funds to meet the District's expected cash needs.

(h) Margin Stock. Suffer or permit the proceeds from any draw under the Letter of Credit, directly or indirectly, to be used (i) to purchase or carry Margin Stock, (ii) to repay or otherwise refinance Debt of the District or others incurred to purchase or carry Margin Stock, (iii) to extend credit for the purpose of purchasing or carrying any Margin Stock, or (iv) to acquire any security in any transaction that is subject to Section 13 or 14 of the Securities Exchange Act of 1934 and regulations promulgated under such Act.

## **ARTICLE VI EVENTS OF DEFAULT**

**SECTION 6.01** Events of Default. The occurrence of any of the following events shall be an "Event of Default" hereunder:

(a) The District shall fail to pay any amount payable under any provision of Article II when due; or

(b) Any representation or warranty made, or deemed made, by or on behalf of the District (or any of its officials) in connection with this Agreement or any of the

Related Documents shall prove to have been incorrect in any material respect when made or deemed made; or

(c) The District shall fail to perform or observe any term, covenant or agreement contained in Section 5.02 hereof on its part to be performed or observed; or

(d) The District shall fail to perform or observe any other term, covenant or agreement contained in any other section of this Agreement on its part to be performed or observed and any such failure shall remain unremedied for ten (10) days after written notice thereof shall have been given to District by the Bank; or

(e) The District shall default in the payment of any Debt (other than Debt arising under this Agreement), whether such Debt now exists or shall hereafter be created, and any period of grace with respect thereto shall have expired, or an event of default as defined in any mortgage, indenture or instrument, under which there may be issued, or by which there may be secured or evidenced, any Debt, whether such Debt now exists or may be hereafter created, shall occur, which default in payment or event of default shall result in such Debt becoming or being declared due and payable prior to the date on which it would otherwise become due and payable; or

(f) An order for relief shall have been entered against the District under the Bankruptcy Code or any other similar applicable Federal or State law, and such decree or order shall have continued undischarged and unstayed for a period of 90 days; or a decree or order of a court having jurisdiction in the premises for the appointment of a receiver, trustee, liquidator or custodian of the District or of its property, or for the winding up or liquidation of its

affairs, shall have been entered, and such decree or order shall have remained in force undischarged and unstayed for a period of 90 days; or

(g) The District shall institute a voluntary case, or shall consent to the institution of an involuntary case against it, or shall file a petition or answer or consent seeking reorganization or arrangement under the Bankruptcy Code or any other similar applicable Federal or State law, or shall consent to the filing of any such petition, or shall consent to the appointment of a receiver, trustee, liquidator or custodian of it or of its property, or shall make an assignment for the benefit of creditors, or shall admit in writing its inability to pay its debts generally as they become due, or corporate action shall be taken by the District in furtherance of any of the aforesaid purposes; or

(h) Any provision of this Agreement or any of the Related Documents to which the District is a party shall at any time for any reason cease to be valid and binding on the District, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the District, or the District shall deny that it has any or further liability or obligation under this Agreement; or

(i) Any “Event of Default” under and as defined respectively in the Trust Agreement, the Installment Sale Agreement or any other Related Document shall have occurred and be continuing; or

(j) Any event which materially and adversely affects the financial condition of the District or the ability of the District to observe and perform the terms of this Agreement shall have occurred and be continuing.

**SECTION 6.02**      **Upon an Event of Default.** If any Event of Default shall

have occurred and be continuing, the Bank may (but shall not be obligated to) by notice to the District, declare the obligation of the Bank to issue the Letter of Credit to be terminated, whereupon the same shall forthwith terminate, or, if the Letter of Credit shall have been issued, (i) give notice to the Trustee pursuant to Section \_\_\_\_ of the Trust Agreement requesting the Trustee to declare a mandatory tender of all Certificates then outstanding and all interest accrued and unpaid thereon to be due and payable, (ii) take such action as may be necessary to cure such Event of Default on behalf and for the account of the District, (iii) require immediate payment in full by the District of any payment or amount owed or to be owed by the District to the Bank hereunder, (iv) exercise any and all of the rights available to it under the Trust Agreement or any Related Documents, and (v) exercise any other rights and remedies available to it at law or in equity or under any other agreement.

It is understood that, upon the occurrence of an Event of Default, the Bank may exercise its rights with respect to remedies available to it under the Trust Agreement or any of the other Related Documents, all without limiting or restricting the Bank's ability, at a later date, to exercise its rights with respect to any remaining revenues for payment of any remaining indebtedness of the District to the Bank.

During the period that an Event of Default has occurred and is continuing, the District shall pay to the Bank the default fee described in Section 2.03(f) hereof.

**ARTICLE VII**  
**MISCELLANEOUS**

**SECTION 7.01**      **USA PATRIOT Act.** The Bank is subject to the USA

PATRIOT Act and hereby notifies the District that pursuant to the requirements of that Act, the Bank is required to obtain, verify and record information that identifies the District, which

information includes the name and address of the District and other information that will allow the Bank to identify the District in accordance with the USA PATRIOT Act.

**SECTION 7.02**      **Amendments, Etc.** This Agreement may be amended only by a written instrument duly executed by each of the parties hereto. The District may take any action herein prohibited or omit to perform any act herein required to be performed by it, only if the District shall first obtain the written consent of the Bank thereto. No course of dealing between the District and the Bank, nor any delay in exercising any rights hereunder, shall operate as a waiver of any rights of the Bank hereunder. Unless otherwise specified in such waiver or consent, a waiver or consent given hereunder shall be effective only in the specific instance and for the specific purpose for which given.

**SECTION 7.03**      **Notices.** All notices, requests and other communications provided for hereunder shall be in electronic, telephonic or written (including bank wire, telegram, telecopier, telex or similar writing) form and shall be given to the party to whom sent, addressed to it, at its address or other address or telephone, telecopier or telex number as such party may hereafter specify for the purpose by notice to the other parties set forth below. Each such notice, request or communication shall be effective (i) if given by telephone, telex, telecopier or other electronic means, when such communication is transmitted to the address specified below and any appropriate answerback is received, (ii) if given by certified or registered mail, return receipt requested, on the date of receipt appearing on the return postal receipt for notices given by certified or registered mail, (iii) if given by hand delivery, when delivered at the address specified below:

(a) if to the District:

Otay Water District  
2554 Sweetwater Springs Boulevard  
Spring Valley, California 91978  
Attention: Mark Walton, General Manager  
Telephone No.: (619) 670-2280  
Telecopier No.: \_\_\_\_\_

(b) if to the Bank:

Union Bank, N.A.  
Public Finance Unit  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
Re: Otay Water District  
Telephone No.: (213) 236-6434  
Telecopier No.: (213) 236-6450

with all reimbursements of Draws on the Letter of Credit wired to:

Union Bank, N.A.  
ABA No. 1220-00496  
Ref: Letter of Credit No. \_\_\_\_\_  
Credit to Account No. 30516196431  
Attention: SC-TSO STANDBY LOC

(c) if to the Trustee:

The Bank of New York Mellon Trust Company, N.A.  
700 South Flower Street, Suite 500  
Los Angeles, California 90017-4104  
Attention: Greg Chenail  
Telephone No.: (213) 630-6229  
Telecopier No.: \_\_\_\_\_

or (iv) in any of the foregoing cases, at such other address or telex, bank wire or telephone number as the addressee may hereafter specify for the purpose in a notice to the other party specifically captioned "Notice of Change of Address pursuant to Section 7.03 of the Reimbursement Agreement."

**SECTION 7.04**      **No Waiver.** Any waiver, consent or approval by the Bank

of any Event of Default or breach of any provision, condition, or covenant of this Agreement or

any Related Document must be in writing and shall be effective only to the extent set forth in writing. No waiver of any breach or default shall be deemed a waiver of any later breach or default of the same or any other provision of this Agreement or any Related Document. No failure or delay on the part of the Bank in exercising any power, right, or privilege under this Agreement or any Related Document shall operate as a waiver thereof, and no single or partial exercise of any such power, right, or privilege shall preclude any further exercise thereof or the exercise of any other power, right or privilege. The Bank has the right at its sole option to continue to accept interest and/or principal payments due under this Agreement or any Related Documents after default, and such acceptance shall not constitute a waiver of said default or an extension of the Maturity Date unless the Bank agrees otherwise in writing.

**SECTION 7.05**      **Rights Cumulative.** All rights and remedies existing under this Agreement and the Related Documents are cumulative to, and not exclusive of, any other rights or remedies available under contract or applicable law.

**SECTION 7.06**      **Right of Set-off.**

(a) Upon the occurrence and during the continuance of any Event of Default, the Bank is hereby authorized at any time and from time to time, to the fullest extent permitted by law, to set off and apply any and all deposits (general or special, time or demand, provisional or final) at any time held and other indebtedness at any time owing by the Bank to or for the credit or the account of the District against any and all of the obligations of the District now or hereafter existing under this Agreement, irrespective of whether or not the Bank shall have made any demand hereunder and although such obligations may be contingent or unmatured.

(b) The Bank agrees promptly to notify the District after any such setoff and application referred to in subsection (a) above, provided that the failure to give such notice shall not affect the validity of such setoff and application. The rights of the Bank under this Section are in addition to other rights and remedies (including, without limitation, other rights of setoff) which the Bank may have.

(c) The Bank agrees that any liens and security interests now or hereafter held by the Bank in property of the District securing the District's obligations hereunder shall be held by the Trustee for the pro rata benefit of the Bank and the Owners of the Certificates, provided, however, that the Bank may exercise its rights with respect to such liens or security interests for its own benefit if (i) it is determined by a court of competent jurisdiction that such exercise would not lead to the Bank's being released, prevented or restrained from or delayed in fulfilling its obligations under the Letter of Credit or (ii) the exercise of such rights with respect to such security interests or liens would not constitute a payment to Owners of the Certificates deemed a voidable preference payment under the Bankruptcy Code or (iii) the exercise of such rights with respect to such security interests or liens would not result in the lowering or suspension by the Rating Agencies of their respective ratings of the Certificates.

**SECTION 7.07**      **Indemnification.** The District shall indemnify and hold the Bank (which, for purposes of this Section, includes the Bank's employees, officers, directors, shareholders, affiliates, correspondents, agents and representatives) harmless from and against any and all claims, actions, proceedings, damages, losses, liabilities, costs or expenses (including but not limited to attorneys' fees and costs) which the Bank may incur or which may be claimed against the Bank by any Person:

(a) by reason of any inaccuracy or alleged inaccuracy in any material respect, or any untrue statement or alleged untrue statement of any material fact, contained in the Official Statement or any amendments or supplements thereto, or by reason of the omission or alleged omission to state therein a material fact necessary to make such statements, in the light of the circumstances under which they were made, not misleading (except that this provision shall not apply to the information contained in the Official Statement describing the Bank); or

(b) by reason of or in connection with the execution, delivery or performance of the Certificates, the Trust Agreement, or any transaction contemplated by the Trust Agreement; or

(c) by reason of or in connection with any of the matters contemplated by this Agreement, any Related Document or the Letter of Credit; or

(d) by reason of or in connection with the execution and delivery or transfer of, or payment or failure to make payment under, the Letter of Credit; provided, however, that the District shall not be required to indemnify the Bank pursuant to this Section 7.07 for any claims, actions, proceedings, damages, losses, liabilities, costs or expenses to the extent caused by the Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Trustee or a successor trustee under the Trust Agreement of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. Nothing in this Section 7.07 is intended to limit the District's obligations contained in Article II. Without prejudice to the survival of any other obligation of the District hereunder, the indemnities and obligations of the District contained in this Section 7.07 shall survive the payment in full of amounts payable pursuant to Article II and termination of the Letter of Credit.

**SECTION 7.08**      **Liability of the Bank.** The District assumes all risks of the

acts or omissions of the Trustee and any other beneficiary or transferee of the Letter of Credit with respect to its use of the Letter of Credit. Neither the Bank nor any of its officers or directors shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or any acts or omissions of the Trustee and any other beneficiary or transferee in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement thereon, even if such documents should prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to such Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except that the District shall have a claim against the Bank, and the Bank shall be liable to the District to the extent of any direct, as opposed to consequential, damages suffered by the District which such District proves were caused by the Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Trustee or a transferee to whom the Letter of Credit has been transferred in accordance with its terms of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. In furtherance and not in limitation of the foregoing, the Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary.

**SECTION 7.09**      **Costs, Expenses and Taxes.** In addition to any other

amounts payable by the District under this Agreement, the District agrees to pay on the Closing Date all costs and expenses of the Bank including, without limitation, the reasonable fees and expenses of counsel for the Bank in connection with the preparation, issuance, or delivery, as the

case may be, of the Letter of Credit, this Agreement, the Related Documents and any other documents that may be delivered in connection with any of the foregoing. In addition, the District agrees to pay promptly all costs and expenses of the Bank (including reasonable counsel fees and expenses) in connection with (i) the filing, recording, administration, transfer, amendment, maintenance, renewal or cancellation of the Letter of Credit, this Agreement, the Related Documents or any other document that the Bank or its counsel reasonably determines that it must review or issue in connection with this Agreement, (ii) any payment by the Bank under the Letter of Credit (without duplication of any of the District's obligations under Section 2.03 hereof) or (iii) any and all stamp and other taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of the Letter of Credit, this Agreement or the Related Documents, and any other documents which may be delivered in connection with this Agreement. In addition, the District agrees to pay promptly all costs and expenses, including without limitation reasonable attorneys' fees and disbursements (and fees and disbursements of the Bank's in-house counsel) expended or incurred by the Bank in any arbitration, mediation, judicial reference, legal action or otherwise in connection with (a) the negotiation, preparation, amendment, interpretation and enforcement of this Agreement and any Related Documents, including without limitation during any workout, attempted workout, and/or in connection with the rendering of legal advice as to the Bank's rights, remedies and obligations under the Related Documents, (b) collecting any sum which becomes due the Bank under this Agreement or any Related Documents, (c) any proceeding for declaratory relief, any counterclaim to any proceeding, or appeal, or (d) the protection, preservation or enforcement of any rights of the Bank. For the purposes of this section, attorneys' fees shall include, without limitation, fees incurred in connection with the following: (1) contempt proceedings; (2)

discovery; (3) any motion, proceeding or other activity of any kind in connection with a bankruptcy proceeding or case arising out of or relating to any petition under Title 11 of the United States Code, as the same shall be in effect from time to time, or any similar law; (4) garnishment, levy, and debtor and third party examinations; and (5) post judgment motions and proceedings of any kind, including without limitation any activity taken to collect or enforce any judgment. The Bank shall give written notice to the District of any amounts as to which the Bank is entitled to reimbursement or indemnification under this Section 7.09, and the District shall pay such amounts to the Bank.

**SECTION 7.10**      **Security Interest in Funds; Limits of Security.** As additional security for payment of its obligations under this Agreement, the District hereby grants a security interest to the Bank in the District's right, title and interest, to the extent thereof, in all funds now or hereafter on deposit in or otherwise a part of any fund held by the Trustee under the Trust Agreement and in the proceeds realized from the investment of any such funds; and the District hereby consents to the Bank's appointment of the Trustee as the Bank's agent to perfect the Bank's security interest in such funds. Except as may be provided in this Agreement and in the other Related Documents, the Bank shall take no right, title or interest in any other funds or property of the District as and for security for the obligations of the District under this Agreement.

**SECTION 7.11**      **Subrogation of the Bank.** From and after payment by the Bank of a draw under the Letter of Credit relating to a payment on the Certificates and until the Bank is paid in full, the District agrees that the Bank shall succeed to all of the right, title and interest of the Trustee and the Owners with respect to the Certificates on which payment was made, despite any discharge and satisfaction of the lien of the Trust Agreement pursuant to the

terms thereof. Such subrogation of the Bank shall constitute additional security and shall not be deemed a substitution for the performance by the District of its obligations hereunder.

**SECTION 7.12**      **Survival of Representations and Warranties.**      All statements contained in any Related Document or in any certificate, financial statement or other instrument delivered by or on behalf of the District pursuant to or in connection with this Agreement (including but not limited to any such statement made in or in connection with any amendment hereto or thereto) shall constitute representations and warranties made under this Agreement. All representations and warranties made under this Agreement (i) shall be made and shall be true at and as of the date of this Agreement, the date the Letter of Credit is issued and the date of each drawing under the Letter of Credit and (ii) shall survive the execution and delivery of this Agreement, regardless of any investigation made by the Bank or on its behalf.

**SECTION 7.13**      **Participations.** The Bank may participate to other banking or financial institutions of the Bank's choosing all or any portion of its obligations under the Letter of Credit and this Agreement (to be evidenced by one or more Participation Agreements or similar documents). The Bank has no obligation to disclose the participation of such other institution. In calculating any amounts owing to the Bank under Section 2.03 hereof, the Participants shall be entitled, subject to the terms thereof, to the payments set forth in Sections 2.07(c) and 2.07(d) as if they were the Bank, to the extent such Participants are affected by the provisions of those Sections. The foregoing notwithstanding, no such participation by the Bank shall in any way affect any of the obligations of the Bank under the Letter of Credit, and the District shall have no obligation to deal in any manner with any such Participant.

**SECTION 7.14**      **Dispute Resolution.** To the extent permitted by law, in connection with any claim, cause of action, proceeding or other dispute concerning the loan

documents (each, a “Claim”), District and the Bank expressly, intentionally and deliberately waive any right each may otherwise have to trial by jury. In the event that the waiver of jury trial set forth in the previous sentence is not enforceable under the law applicable to this Agreement, District and the Bank agree that any Claim, including any question of law or fact relating thereto, shall, at the written request of District or the Bank, be determined by judicial reference pursuant to the law applicable to this Agreement. District and the Bank shall select a single neutral referee, who shall be a retired state or federal judge. In the event that District and the Bank cannot agree upon a referee, the court shall appoint the referee. The referee shall report a statement of decision to the court. Nothing in this Section 7.14 shall limit the right of District or the Bank at any time to exercise self-help remedies, foreclose against collateral or obtain provisional remedies. District and the Bank shall bear the fees and expenses of the referee equally, unless the referee orders otherwise. The referee shall also determine all issues relating to the applicability, interpretation and enforceability of this paragraph. District and the Bank acknowledge that if a referee is selected to determine the Claims, then the Claims will not be decided by a jury.

**SECTION 7.15      Binding Effect.** This Agreement shall become effective when it shall have been executed by the District and the Bank and thereafter shall be binding upon and inure to the benefit of the District and the Bank and their respective successors and assigns, except that the District shall not have the right to assign its rights hereunder or any interest herein without the prior written consent of the Bank.

**SECTION 7.16      Severability.** Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without

invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

**SECTION 7.17**      **Governing Law.** This Agreement shall be governed by, and construed in accordance with, the laws of the State.

**SECTION 7.18**      **Headings.** Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

**SECTION 7.19**      **Execution in Counterparts.** It shall not be necessary that all parties execute and deliver the same counterpart of this Agreement. This Agreement shall therefore become effective when each party has executed any counterpart hereof and delivered the same to the other parties. All such counterparts, collectively, shall be deemed a single agreement.

**SECTION 7.20**      **Electronic Execution of Assignment and Certain Other Documents.** The words “execution,” “signed,” “signature,” and words of like import in any amendment or other modification hereof (including waivers and consents) shall be deemed to include electronic signatures or the keeping of records in electronic form, each of which shall be of the same legal effect, validity or enforceability as a manually executed signature or the use of a paper-based recordkeeping system, as the case may be, to the extent and as provided for in any applicable law, including the Federal Electronic Signatures in Global and National Commerce Act, the New York State Electronic Signatures and Records Act, or any other similar state laws based on the Uniform Electronic Transactions Act.

**SECTION 7.21**      **Assignment to Federal Reserve Bank.** The Bank may assign and pledge all or any portion of the Obligations owing to it to any Federal Reserve Bank

or the United States Treasury as collateral security pursuant to Regulation A of the Board of Governors of the Federal Reserve System and any Operating Circular issued by such Federal Reserve Bank, *provided* that any payment in respect of such assigned Obligations made by the Corporation to the Bank in accordance with the terms of this Agreement shall satisfy the Corporation's Obligations hereunder in respect of such assigned Obligation to the extent of such payment. No such assignment shall release the Bank from its obligations hereunder.

**IN WITNESS WHEREOF**, the parties hereto have caused this Agreement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

**OTAY WATER DISTRICT**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

**UNION BANK, N.A.**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

**EXHIBIT A  
TO REIMBURSEMENT AGREEMENT**

**IRREVOCABLE LETTER OF CREDIT**

No. \_\_\_\_\_

\_\_\_\_\_, 2011

The Bank of New York Mellon Trust Company, N.A.  
as Trustee  
700 South Flower Street, Suite 500  
Los Angeles, California 90071-4104  
Attention: Greg Chenail

Dear Sirs:

We hereby establish, at the request and for the account of Otay Water District (the "District"), in your favor, as Trustee under the Trust Agreement, dated as of June 1, 1996 (the "Trust Agreement") among the District, Otay Service Corporation and you, pursuant to which \$15,400,000 in aggregate principal amount of the District's Certificates of Participation (the "Certificates"), were executed and delivered, our Irrevocable Letter of Credit No. \_\_\_\_\_, in the amount of \$\_\_\_\_\_, effective immediately and expiring at the close of banking business at our Monterey Park office referred to below on \_\_\_\_\_, 2014 or on such later date to which such expiration date may be extended from time to time by amendment of this Letter of Credit (the "Maturity Date"), unless terminated earlier pursuant to the terms hereof.

We hereby irrevocably authorize you to draw on us, in an aggregate amount not to exceed the amount of this Letter of Credit as set forth above and in accordance with the terms and conditions and subject to the reductions in amount as hereinafter set forth,

- (1) in one or more drawings by one or more of your drafts (in the form of Exhibit 1 attached hereto), each drawn on us payable at sight on a Banking Day, and accompanied by your written and completed certificate signed by you in substantially the form of Annex A attached hereto (such draft accompanied by such certificate being your "Payment Draft"); and
- (2) in one or more drawings by one or more of your drafts (in the form of Exhibit 1 attached hereto), each drawn on us payable at sight on a Banking Day, and accompanied by your written and completed certificate signed by you in substantially the form of Annex B attached hereto (any such draft accompanied by such certificate being your "Tender Draft").

The Payment Draft accompanied by a certificate in substantially the form of Annex A attached hereto with the first box in paragraph (2), entitled "Interest Drawing," checked shall be hereinafter referred to as Interest Draft; the Payment Draft accompanied by a certificate in substantially the form of Annex A attached hereto with the second box in paragraph (2), entitled "Partial Prepayment Drawing," checked shall be hereinafter referred to as Partial Prepayment Draft; and the Payment Draft accompanied by a certificate in substantially the form of Annex A attached hereto with the third box in paragraph (2), entitled "Final Drawing," checked shall be hereinafter referred to as Final Draft. The amount of each Interest Draft shall not exceed \$\_\_\_\_\_, the aggregate amount of Partial Prepayment Drafts shall not exceed \$\_\_\_\_\_ and the amount of the Final Draft shall not exceed \$\_\_\_\_\_.

### REDUCTIONS AND REINSTATEMENTS

If you shall draw on us by your Interest Draft under clause (1) of the immediately preceding paragraph and you shall not have received from us, by the close of business on the fifth Banking Day following the date of such drawing, a notice to the effect that we have not been reimbursed for such drawing and that accordingly the interest portion of this Letter of Credit will not be reinstated for the amount of such drawing, your right to draw on us in a single drawing by your Interest Draft under said clause (1) shall be automatically reinstated along with the amount drawn on us by your Interest Draft and, effective the sixth Banking Day from the date of such drawing, you shall again be authorized to draw on us by your Interest Draft in accordance with said clause (1) and the other terms and conditions referred to or set forth in the immediately preceding paragraph; and this automatic reinstatement of your right to draw on us by your Interest Draft as well as the reinstatement of the amount drawn on us by your Interest Draft shall be applicable to successive drawings by your Interest Drafts under clause (1) of the immediately preceding paragraph so long as this Letter of Credit shall not have terminated as set forth below.

The amount of this Letter of Credit shall be decreased, upon our receipt of your written and completed certificate signed by you in substantially the form of Annex C attached hereto (relating to a redemption or defeasance of less than all the Certificates outstanding), by an amount equal to the amount stated in said certificate, and the amounts available to be drawn by you by any subsequent Payment Draft or Tender Draft shall be decreased, upon our receipt of such certificate, to the amounts stated in such certificate.

Upon our honoring any Tender Draft or Partial Prepayment Draft presented by you hereunder, the amount of this Letter of Credit and the amounts available to be drawn hereunder by you by any subsequent Tender Draft, Partial Prepayment Draft or Final Draft shall be automatically decreased by an amount equal to the amount of such Tender Draft or Partial Prepayment Draft. The amount of this Letter of Credit and the amounts from time to time available to be drawn by you hereunder by any subsequent Tender Draft, Partial Prepayment Draft or Final Draft shall be increased when and to the extent, but only when and to the extent, that we are reimbursed by the District or by you on behalf of the District for any amount drawn hereunder by any Tender Draft. Any amount received by us from or on behalf of the District in reimbursement of amounts drawn hereunder shall, if we also receive your certificate completed and signed by you in substantially the form of Annex D attached hereto, be applied to the extent

of the amount indicated therein to reimburse us for amounts drawn hereunder by your Tender Drafts.

### PRESENTMENT

Funds under this Letter of Credit are available to you against (1) your Interest Draft referring thereon to the number of this Letter of Credit and accompanied by your written and completed certificate signed by you in substantially the form of Annex A attached hereto with the first box in paragraph (2), entitled "Interest Drawing," checked, (2) your Tender Draft referring thereon to the number of this Letter of Credit and accompanied by your written and completed certificate signed by you in substantially the form of Annex B attached hereto, (3) your Partial Prepayment Draft referring thereon to the number of this Letter of Credit and accompanied by your written and completed certificate signed by you in substantially the form of Annex A attached hereto with the second box in Paragraph (2), entitled "Partial Prepayment Drawing," checked, and (4) your Final Draft referring thereon to the number of this Letter of Credit and accompanied by your written and completed certificate signed by you in substantially the form of Annex A attached hereto with the third box in paragraph (2), entitled "Final Drawing," checked. Each such draft and certificate shall be presented at our office (the "Bank's Office") located at 1980 Saturn Street, Monterey Park, California 91755-7417, Attention: SC-TSO, Standby Letters of Credit, V02-906 (or at any other office which may be designated by us by written notice delivered to you) on or before the day (which shall be a Banking Day) of our making funds available to you hereunder, but in no event, later than 9:00 a.m. (Pacific time) on the day of our making funds available to you. If we receive any of your drafts and Certificates at such office, all in strict conformity with the terms and conditions of this Letter of Credit, not later than 9:00 a.m. (Pacific time) on a Banking Day up to and including the Stated Termination Date hereof, we will honor the same on the same day (not later than 11:00 a.m. Pacific time). If we receive any of your drafts and certificates at such office, all in strict conformity with the terms and conditions of this Letter of Credit, after 9:00 a.m. (Pacific time) on a Banking Day, but prior to 5:00 p.m. (Pacific time), up to and including the Stated Termination Date hereof, we will honor the same on the next succeeding Banking Day (not later than 10:00 a.m., Pacific time) in accordance with your payment instructions. Your certificate may indicate a later date on which your draft is to be honored in which case, if your drafts and certificates are in strict conformity with the terms and conditions of this Letter of Credit, we will honor the same not later than 10:00 a.m. Pacific time on the date you requested in accordance with your payment instructions, provided that such date is a Banking Day and occurs prior to the Maturity Date.

Drafts to be presented hereunder, including the required Annexes, may be presented by telecommunications through telefax number (323) 720-2773 and the Bank shall be entitled to rely thereon as if such Drafts and certificates were presented in person, provided such Drafts, including the required certificates, are in conformance with the requirements for the same as set forth herein, but for the requirement of an original signature, with originally executed Drafts and certificates to follow immediately thereafter, via overnight mail or courier service. The Bank shall have no duty and will not examine original documents confirming presentation by telecommunications. In the event of presentation by telecommunications, the telecommunication is considered the sole original presentation.

All payments made by us under this Letter of Credit will be made in immediately available funds and will be disbursed from our own funds. If requested by you, payment under this Letter of Credit may be made by wire transfer of Federal Reserve Bank of San Francisco funds to your account in a bank on the Federal Reserve wire system.

#### EXPIRATION

Upon the earliest of (i) the date on which we receive written notice from you that there are no longer any Certificates "Outstanding" within the meaning of the Trust Agreement, (ii) the date on which we honor a Final Draft and (iii) the Maturity Date, this Letter of Credit shall automatically terminate ("Stated Termination Date").

#### TRANSFER

This Letter of Credit is transferable in its entirety only to any transferee who you certify to us has succeeded or replaced you as Trustee under the Trust Agreement and, notwithstanding Article 38 of the UCP, defined below, may be successively transferred. Transfer of the available balance under this Letter of Credit to such transferee shall be effected by the presentation to us of this Letter of Credit and any amendments thereto, accompanied by a completed certificate in the form of Annex E attached hereto. Upon such presentation we shall issue a letter of credit to your transferee with provisions therein consistent with this Letter of Credit, excepting only necessary changes as to:

1. Identity and address of your transferee, as beneficiary;
2. The date thereof; and
3. The amount.

#### GOVERNING LAW

This Letter of Credit is subject to the Uniform Customs and Practice for Documentary Credits (2007 Revision), International Chamber of Commerce, Publication No. 600), except for Articles 32 and 38. For purposes of Article 6(d), the place of presentation for payment shall be the Bank's Office. In addition, the Bank agrees, notwithstanding the second sentence of Article 36, if the Maturity Date occurs upon a Banking Day on which the Bank's Office is closed by virtue of an interruption of the nature described in Article 36, the Maturity Date will be extended to the next Banking Day on which the Bank's Office is open. As to matters not governed thereby, this Letter of Credit shall be governed by the laws of the State of California, including the Uniform Commercial Code as in effect in the State of California.

#### MISCELLANEOUS

This Letter of Credit sets forth in full our undertaking and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein (including, without limitation, the Certificates, except only the certificates and the drafts referred to herein; and any such reference shall not be deemed

to incorporate herein by reference any document, instrument or agreement except for such certificates and such drafts.

For all purposes of this Letter of Credit, the term "Banking Day" means any day other than a Saturday, Sunday or other day on which banks are authorized or required to be closed in the State of California.

Communications with respect to this Letter of Credit shall be in writing and shall be addressed to us at 1980 Saturn Street, Monterey Park, California 91755-7417, Attention: SC-TSO, Standby Letters of Credit, V02-906 (Phone: (323) 720-7957) with a copy to us at 445 South Figueroa Street, G08-268, Los Angeles, California 90071, specifically referring to the number of this Letter of Credit.

Very truly yours,

**UNION BANK, N.A.**

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

Exhibit 1

Date: \_\_\_\_\_

Amount: \$ \_\_\_\_\_

Drawn under Union Bank, N.A.  
Irrevocable Letter of Credit No. \_\_\_\_\_

Union Bank, N.A.  
Southern California  
Trade Service Operations  
1980 Saturn Street, V02-906  
Monterey Park, California 91755-7417  
Attn: Standby Letter of Credit Section

At sight, please pay to the order of the undersigned the amount of [ \_\_\_\_\_ ]  
and no/100 Dollars (\$ \_\_\_\_\_ .00).

\_\_\_\_\_, as Trustee

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

Annex A

PAYMENT DRAWING

To: Union Bank, N.A.  
1980 Saturn Street  
Monterey Park, California 91755-7417  
Attention: SC-TSO, Standby Letters of Credit, V02-906

Re: Irrevocable Letter of Credit No, \_\_\_\_\_

The undersigned, a duly authorized officer of the undersigned Trustee (the "Trustee"), hereby certifies to Union Bank, N.A. (the "Bank"), with reference to Irrevocable Letter of Credit No. \_\_\_\_\_ (the "Letter of Credit"), issued by the Bank in favor of the Trustee, as follows:

(1) The Trustee is the Trustee under the Trust Agreement.

\*(2)  Interest Drawing.

(i) The Trustee is making a drawing under the Letter of Credit with respect to a payment of interest on the Certificates, which payment is due on the day on which this certificate and the Interest Draft it accompanies are being presented to the Bank, if presented not later than 9:00 a.m. (Pacific time), or on the next Banking Day after such day unless a later date is specified as follows for payment: \_\_\_\_\_. None of such Certificates is a Bank Certificates and more is held of record by the District or the Corporation or by the undersigned for the account of the District or the Corporation.

(ii) [The Interest Draft accompanying this certificate is the first Interest Draft presented by the Trustee under the Letter of Credit.]\*\* [The Interest Draft last presented by the Trustee under the Letter of Credit was honored and paid by the Bank and the Trustee did not, within five Banking Days, receive a notice from the Bank that the Bank has not been reimbursed.]\*\*\*

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\* Please check a box as appropriate.

\*\* To be used in the Draw Certificate relating to the first Interest Draft only.

\*\*\* To be used in each Draw Certificate relating to each Interest Draft other than the first Interest Draft.

The amount of the Interest Draft accompanying this certificate is \$\_\_\_\_\_. It was computed in compliance with the terms and conditions of the Certificates and the Trust Agreement and does not include any amount of interest which is included in any Tender Draft, Partial Prepayment Draft or Final Draft presented on or prior to the date of this certificate.

Partial Prepayment Drawing.

(i) The Trustee is making a drawing under the Letter of Credit with respect to the payment, upon redemption or prepayment of less than all of the Certificates, of the unpaid principal amount of, and up to \_\_\_ days' accrued and unpaid interest on, Certificates which are Outstanding within the meaning of the Trust Agreement (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation), which payment is due on the day on which this certificate and the Partial Prepayment Draft it accompanies are being presented to the Bank, if presented not later than 9:00 a.m. (Pacific time), or on the next Banking Day after such day unless a later date is specified as follows for payment: \_\_\_\_\_.

(ii) The amount of the Partial Prepayment Draft accompanying this certificate is equal to the sum of (i) \$\_\_\_\_\_ being drawn in respect of the payment of unpaid principal of Certificates (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation) to be redeemed or prepaid and (ii) \$\_\_\_\_\_ being drawn in respect of the payment of accrued and unpaid interest on such Certificates, and does not include any amount of interest on the Certificates which is included in any Interest Draft where the interest was not reinstated or Tender Draft or Partial Prepayment Draft presented on or prior to the date of this certificate.

(iii) The amount of the Partial Prepayment Draft accompanying this certificate was computed in accordance with the terms and conditions of the Certificates and the Trust Agreement and does not exceed the amount available to be drawn under the Letter of Credit.

(iv) The Trustee acknowledges that pursuant to the terms of the Letter of Credit, upon the Bank's honoring the Partial Prepayment Draft accompanying this certificate, the amount of the Letter of Credit and the amounts available to be drawn by the Trustee thereunder by any subsequent Partial Prepayment Draft or Tender Draft or Final Draft are automatically decreased by an amount equal to the amount of such Partial Prepayment Draft.

Final Drawing.

(i) The Trustee is making a drawing under the Letter of Credit with respect to the payment, either at stated maturity, upon acceleration or as a result of

a prepayment, redemption or mandatory tender, of the unpaid principal amount of, and up to \_\_\_\_ days' accrued and unpaid interest on, all of the Certificates which are Outstanding within the meaning of the Trust Agreement (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation) but which are not to be remarketed again with the support of the Letter of Credit, which payment is due on the day on which this certificate and the Final Draft it accompanies are being presented to the Bank, if presented not later than 9:00 a.m. (Pacific time), or on the next Banking Day after such day unless a later date is specified as follows for payment: \_\_\_\_\_.

(ii) The amount of the Final Draft accompanying this certificate is equal to the sum of (i) \$\_\_\_\_\_ being drawn in respect of the payment of unpaid principal of Certificates (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation) and (ii) \$\_\_\_\_\_ being drawn in respect of the payment of accrued and unpaid interest on such Certificates, and does not include any amount of interest on the Certificates which is included in any Interest Draft where the interest was not reinstated or Tender Draft or Partial Prepayment Draft presented on or prior to the date of this certificate.

(iii) The amount of the Final Draft accompanying this certificate was computed in compliance with the terms and conditions of the Certificates and the Trust Agreement and does not exceed the amount available to be drawn by the Trustee under the Letter of Credit.

The terms used herein which are not specifically defined herein are defined in the Letter of Credit.

IN WITNESS WHEREOF, the Trustee has executed and delivered this certificate as of the \_\_\_\_\_ day of \_\_\_\_\_.

\_\_\_\_\_  
\_\_\_\_\_  
as Trustee

By \_\_\_\_\_  
[Name and Title]

cc: Public Finance Unit  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
(Failure to deliver this copy will  
not invalidate the Draft)

Annex B

TENDER DRAWING

To: Union Bank, N.A.  
1980 Saturn Street  
Monterey Park, California 91755-7417  
Attention: SC-TSO, Standby Letters of Credit, V02-906

Re: Irrevocable Letter of Credit No. \_\_\_\_\_

The undersigned, a duly authorized officer of the Trustee (the "Trustee"), hereby certifies to Union Bank, N.A. (the "Bank"), with reference to irrevocable Letter of Credit No. \_\_\_\_\_ (the "Letter of Credit"), issued by the Bank in favor of the Trustee, as follows:

(1) The Trustee is the Trustee under the Trust Agreement.

(2) The Trustee is making a drawing under the Letter of Credit with respect to the payment, upon a tender, of the unpaid principal amount of, and accrued and unpaid interest on, all or less than all of the Certificates which are Outstanding within the meaning of the Trust Agreement to be purchased as a result of such tender (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation), which payment is due on the day on which this certificate and the Tender Draft it accompanies are being presented to the Bank, if presented not later than 9:00 a.m. (Pacific time), or on the next Banking Day after such day unless a later date is specified as follows for payment: \_\_\_\_\_.

(3) The amount of the Tender Draft accompanying this certificate is equal to the sum of (i) \$\_\_\_\_\_ being drawn in respect of the payment of unpaid principal of Certificates (other than Bank Certificates or Certificates presently held of record by the District or the Corporation or by the Trustee for the account of the District or the Corporation) to be purchased as a result of a tender and (ii) \$\_\_\_\_\_ being drawn in respect of the payment of accrued and unpaid interest on such Certificates, and does not include any amount of interest which is included in any Interest Draft where the interest was not reinstated or Partial Prepayment Draft presented on or prior to the date of this certificate.

(4) The amount of the Tender Draft accompanying this certificate was computed in compliance with the terms and conditions of the Certificates and the Trust Agreement and does not exceed the amount available to be drawn under the Letter of Credit.

The undersigned acknowledges that pursuant to the terms of the Letter of Credit, upon the Bank's honoring of the Tender Draft accompanying this certificate, the amount of the Letter of Credit and the amounts available to be drawn thereunder by any subsequent Tender Draft or Partial Prepayment Draft or Final Draft are automatically decreased by an amount equal to the amount of such Tender Draft.

The terms used herein which are not specifically defined herein are defined in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed and delivered this certificate as of the \_\_\_\_\_ day of \_\_\_\_\_.

\_\_\_\_\_

\_\_\_\_\_ as Trustee

By \_\_\_\_\_  
[Name and Title]

cc: Public Finance Unit  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
(Failure to deliver this copy will  
not invalidate the Draft)

Annex C

CERTIFICATE FOR REDUCTION

To: Union Bank, N.A.  
1980 Saturn Street  
Monterey Park, California 91755-7417  
Attention: SC-TSO, Standby Letters of Credit, V02-906

Re: Irrevocable Letter of Credit No. \_\_\_\_\_

The undersigned, a duly authorized officer of the undersigned Trustee (the "Trustee"), hereby certifies to Union Bank, N.A. (the "Bank"), with reference to Irrevocable Letter of Credit No. \_\_\_\_\_ (the "Letter of Credit"), issued by the Bank in favor of the Trustee, as follows:

(1) The Trustee is the Trustee under the Trust Agreement.

(2) The Trustee hereby notifies you that on or prior to the date hereof \$\_\_\_\_\_ principal amount of the Certificates has been redeemed and paid or has been defeased pursuant to the Trust Agreement.

(3) Following the redemption, payment or defeasance referred to in paragraph (2) above, the aggregate principal amount of all of the Certificates which are "Outstanding" within the meaning of the Trust Agreement is \$\_\_\_\_\_.

(4) The maximum amount of interest, computed in accordance with the terms and conditions of the Certificates and the Trust Agreement, which could accrue on the Certificates referred to in paragraph (3) above is \$\_\_\_\_\_.

(5) The amount available to be drawn by the Trustee under the Letter of Credit by any Interest Draft is reduced to \$\_\_\_\_\_ (such amount being equal to the amount specified in paragraph (4) above) upon receipt by the Bank of this certificate.

(6) The amount available to be drawn by the Trustee under the Letter of Credit by any Tender Draft or Partial Prepayment Draft or Final Draft is reduced to \$\_\_\_\_\_ (such amount being equal to the sum of the amounts specified in paragraphs (3) and (4) above) upon receipt by the Bank of this certificate.

(7) The amount of the Letter of Credit is reduced to \$\_\_\_\_\_ (such amount equal to the sum of the amounts specified in paragraph (6) above) upon receipt by the Bank of this certificate.

The terms used herein which are not specifically defined herein are defined in the Letter of Credit.

IN WITNESS WHEREOF, the Trustee has executed and delivered this certificate this \_\_\_\_\_ day of \_\_\_\_\_.

\_\_\_\_\_

\_\_\_\_\_ as Trustee

By \_\_\_\_\_  
[Name and Title]

cc: Public Finance Unit  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
(Failure to deliver this copy will  
not invalidate the Draft)

Annex D

CERTIFICATE FOR REINSTATEMENT

To: Union Bank, N.A.  
1980 Saturn Street  
Monterey Park, California 91755-7417  
Attention: SC-TSO, Standby Letters of Credit, V02-906

Re: Irrevocable Letter of Credit No. \_\_\_\_\_

The undersigned, a duly authorized officer of the undersigned Trustee (the "Trustee"), hereby certifies to Union Bank, N.A. (the "Bank"), with reference to Irrevocable Letter of Credit No. \_\_\_\_\_ (the "Letter of Credit"), issued by the Bank in favor of the Trustee, as follows:

(1) The Trustee is the Trustee under the Trust Agreement.

(2) The amount of \$ \_\_\_\_\_ paid to you today by the \_\_\_\_\_ or by the Trustee on behalf of the \_\_\_\_\_ is a payment made to reimburse you for amounts drawn under the Letter of Credit by Tender Drafts and is the amount by which the Letter of Credit is to be reinstated.

(3) Of the amount referred to in paragraph (2), \$ \_\_\_\_\_ represents the aggregate principal amount of Certificates resold or to be resold on behalf of the \_\_\_\_\_.

(4) Of the amount referred to in paragraph (2), \$ \_\_\_\_\_ represents accrued and unpaid interest on Certificates calculated in accordance with the Trust Agreement.

The terms used herein which are not specifically defined herein are defined in the Letter of Credit.

IN WITNESS WHEREOF, the Trustee has executed and delivered this certificate this \_\_\_\_\_ day of \_\_\_\_\_.

\_\_\_\_\_  
\_\_\_\_\_  
as Trustee

By \_\_\_\_\_  
[Name and Title]

cc: Public Finance Unit  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
(Failure to deliver this copy  
will not invalidate the Draft)

Annex E

INSTRUCTION TO TRANSFER

\_\_\_\_\_ 20\_\_

To: Union Bank, N.A.  
1980 Saturn Street  
Monterey Park, California 91755-7417  
Attention: SC-IOC, Standby Letters of Credit, V02-906

Re: Irrevocable Letter of Credit No. \_\_\_\_\_

Gentlemen:

For value received, the undersigned beneficiary hereby irrevocably transfers to:

\_\_\_\_\_  
[Name of Transferee]

\_\_\_\_\_  
[Address]

all rights of the undersigned beneficiary to draw under the above-captioned Letter of Credit (the "Letter of Credit"). The transferee has succeeded or replaced the undersigned as Trustee under the Trust Agreement (as defined in the Letter of Credit).

By this transfer, all rights of the undersigned beneficiary in the Letter of Credit are transferred to the transferee and the transferee shall hereafter have the sole rights as beneficiary thereof; provided, however, that no rights shall be deemed to have been transferred to the transferee until the transfer fee of \$2000 is paid to you.

The Letter of Credit is returned herewith and in accordance therewith we ask that this transfer be effective and that you issue a new irrevocable letter of credit in favor of the transferee with provisions consistent with the Letter of Credit.

\_\_\_\_\_  
\_\_\_\_\_  
as predecessor Trustee

By \_\_\_\_\_  
[Name and Title]

cc: Union Bank, N.A.  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071  
(Failure to deliver this copy  
will not invalidate the Draft)

**EXHIBIT B  
TO REIMBURSEMENT AGREEMENT**

**CUSTODY AGREEMENT**

This CUSTODY AGREEMENT is made as of June 1, 2011, by and between UNION BANK, N.A., a national banking association organized and existing under the laws of the United States (the "Bank"), and THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A. (the "Custody Agent").

**RECITALS**

WHEREAS, pursuant to the terms and conditions set forth in that certain Reimbursement Agreement, dated as of June 1, 2011 (the "Reimbursement Agreement") by and between the Otay Water District (the "District") and the Bank, the Bank has agreed to issue its irrevocable Letter of Credit (as defined in the Reimbursement Agreement), for the account of the District in connection with \$15,400,000 in Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates") executed and delivered under that certain Trust Agreement dated as of June 1, 1996 (the "Trust Agreement") among the District, Chemical Trust Company of California as trustee (succeeded by The Bank of New York Mellon Trust Company, N.A.) (the "Trustee"), and Otay Service Corporation (the "Corporation") (all other terms used herein which are defined in the Reimbursement Agreement and not defined herein shall have the same meanings assigned to them in the Reimbursement Agreement, unless the context otherwise requires); and

WHEREAS, pursuant to the terms and conditions set forth in the Reimbursement Agreement, in the event that the Letter of Credit is drawn upon to pay the purchase price of Certificates tendered in accordance with the Trust Agreement, such Certificates will be delivered

to, owned by and registered in the name of the Bank (the "Bank Certificates"), until such time as the Bank Certificates are remarketed or cancelled and the Bank is reimbursed for all amounts due under the Reimbursement Agreement; and

WHEREAS, the Bank hereby wishes to appoint the Custody Agent as its agent to take possession of and hold the Bank Certificates on behalf of and for the benefit of the Bank, on the terms and under the conditions set forth in this Custody Agreement, and the Custody Agent is willing to do so.

NOW, THEREFORE, in consideration of the mutual covenants recited herein, and for other good and valuable consideration, the receipt of which is hereby acknowledged, it is hereby agreed as follows:

1. The Bank hereby appoints the Custody Agent as its agent and bailee for the purpose of receiving Bank Certificates and holding such Bank Certificates for and on behalf of the Bank. The Custody Agent hereby agrees to hold the Bank Certificates for such purpose, as the Bank's agent and bailee.

2. Except at the written direction of the Bank, the Custody Agent shall not pledge, hypothecate, transfer or release possession of any Bank Certificates held by the Custody Agent on behalf of the Bank to any person or in any manner not in accordance with this Custody Agreement, and the Custody Agent shall not enter into any other agreement regarding the possession of the Bank Certificates without the prior written consent of the Bank. The Custody Agent shall be entitled to release remarketed Bank Certificates in its custody in accordance with and as contemplated by the Trust Agreement; provided that it (a) holds for the account of the Bank (i) the aggregate principal amount of the Certificates resold plus (ii) the aggregate amount of interest on such principal amount which was paid by the applicable Tender Agent; and (b) the

Custody Agent, as trustee, delivers to the Bank, as Trustee, a completed and signed certificate substantially in the form of Annex D to the Letter of Credit.

3. This Custody Agreement cannot be amended or modified except in a writing signed by the Custody Agent and the Bank.

4. This Custody Agreement shall inure to the benefit of and shall be binding upon the Custody Agent and the Bank, and their respective successors and assigns.

5. Upon written notice to the Bank, and the release to the Bank or its designee of any Bank Certificates then held by the Custody Agent pursuant to this Custody Agreement, the Custody Agent shall have the right to terminate its obligations under this Custody Agreement.

6. Beyond its duties as to the custody of the Bank Certificates expressly provided herein, the Custody Agent shall not have any duty to the Bank as to any Bank Certificates in the Custody Agent's possession or control, or in the possession or control of any of the Custody Agent's agents or nominees, or as to any income thereon or as to the preservation of rights against prior parties or any other rights pertaining thereto. In performing its duties under this Custody Agreement, the Custody Agent shall not be liable to the Bank except for gross negligence or willful misconduct in the performance of its obligations hereunder.

7. The Bank shall indemnify and hold harmless the Custody Agent against any and all liability arising out of the Custody Agent's performance of its obligations hereunder, except due to gross negligence or willful misconduct of the Custody Agent.

8. The Custody Agent may rely and shall be protected in acting or refraining from acting in good faith upon any written notice, instruction or request furnished to it hereunder and believed by it to be genuine and to have been signed and presented to it by the proper party.

9. The Custody Agent agrees to maintain the Custody Agreement without charge to the Bank, so long as it acts as Tender Agent with respect to the Certificates.

10. This Custody Agreement shall be governed by, and construed in accordance with, the laws of the State of California.

11. It shall not be necessary that all parties execute and deliver the same counterpart of this Agreement. This Agreement shall therefore become effective when each party has executed any counterpart hereof and delivered the same to the other parties. All such counterparts, collectively, shall be deemed a single agreement.

12. The Bank acknowledges that the Custody Agent is acting as Trustee under the Trust Agreement. The Bank agrees that nothing contained in this Custody Agreement shall be construed to require the Custody Agent to do any act or omit to do any act contrary to the duties of the Trustee under the Trust Agreement.

IN WITNESS WHEREOF, the parties hereto have hereunto set their hands by their authorized representatives, all as of the date above first written.

THE BANK OF NEW YORK MELLON  
TRUST COMPANY, N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

UNION BANK, N.A.

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

EXHIBIT C  
TO REIMBURSEMENT AGREEMENT

OPINION OF COUNSEL TO DISTRICT

[Date of Issuance of  
Letter of Credit]

Union Bank, N.A.  
445 South Figueroa Street, G08-268  
Los Angeles, California 90071

Re: Reimbursement Agreement between Union Bank  
and Otay Water District

Gentlemen:

We have acted as counsel to Otay Water District (the "District"). We are familiar with the matters relating to the preparation, execution and delivery of a Reimbursement Agreement, dated as of June 1, 2011 (the "Reimbursement Agreement"), between the District and you (the "Bank"). Terms defined in the Reimbursement Agreement are used herein as therein defined. Among other things, we have examined:

- (1) a fully executed counterpart of the Reimbursement Agreement;
- (2) the Letter of Credit referred to in the Reimbursement Agreement;
- (3) the by-laws of the District as now in effect (the "By-laws"); and
- (4) the documents delivered by or on behalf of the District pursuant to Section 3.01 of the Reimbursement Agreement.

We have also examined the originals, or copies certified to our satisfaction, of (i) such other corporate records of the District, certificates of public officials and of officers of the District, (ii) the agreements, instruments and documents which affect or purport to affect the obligations of the District under the Reimbursement Agreement, and (iii) such other agreements, instruments and documents as we have deemed necessary as a basis for the opinions hereinafter expressed. As to questions of fact material to such opinions, we have, when relevant facts were not independently established by us, relied upon certificates of the District or its officers or of public officials. We have assumed the due execution and delivery of the Reimbursement Agreement by the Bank.

Based upon the foregoing and upon such investigation as we have deemed necessary, we are of the opinion that:

1. The District is a water district duly organized and existing under the Constitution and laws of the State of California.

2. The execution, delivery and performance by the District of the Reimbursement Agreement and the Related Documents to which it is a party are within the District's powers, have been duly authorized by necessary governmental action, do not contravene (i) applicable law or (ii) any contractual restriction binding on or affecting the District, and do not result in or require the creation of any lien, security interest or other charge or encumbrance (except as provided in or contemplated by the Reimbursement Agreement or the Trust Agreement) upon or with respect to any of its properties.

3. No authorization or approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due execution, delivery and performance by the District of the Reimbursement Agreement or any Related Document to which it is a party.

4. The Reimbursement Agreement and the Related Documents to which the District is a party have been duly executed and delivered by the District and are the legal, valid and binding obligations of the District enforceable against the District in accordance with their respective terms.

5. There is no pending or, to the best of our knowledge after due inquiry, threatened action, investigation or proceeding against or affecting the District before any court, governmental agency or arbitrator which may materially adversely affect the financial condition or operations of the District or the ability of the District to perform its obligations under the Reimbursement Agreement or any Related Document or which purports to affect the legality, validity or enforceability of the Reimbursement Agreement or any Related Document.

6. The Installment Sale Agreement and the Installment Payments payable thereunder have been duly assigned and validly pledged to the Trustee as security for the payment and performance of the District's obligations under the Trust Agreement and the Reimbursement Agreement and no further action or filings are required of the Bank or any other person to perfect the interest of the Bank in such Installment Sale Agreement and such Installment Payments.

7. The Certificate Holders and the Bank have a perfected lien on and security interest in all monies in the funds held by the Trustee under the Trust Agreement and no further action or filings are required of the Bank or any other person to perfect the interest of the Bank in such monies.

The opinions set forth above are subject to the following qualifications:

(a) The enforceability of the District's obligations under the Reimbursement Agreement and the Related Documents is subject to the effect of applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(b) The enforceability of the District's obligations under the Reimbursement Agreement and the Related Documents may be subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

In addition to the foregoing, we hereby authorize and permit you to rely on our opinion of June \_\_, 2011, addressed to \_\_\_\_\_ and rendered in connection with the issuance of the Certificates.

Very truly yours,

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Exhibit A – Letter of Credit

Exhibit B – Custody Agreement

Exhibit C – Opinion of Counsel to District

**BOND COUNSEL AGREEMENT****OTAY WATER DISTRICT****VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION  
(1996 CAPITAL PROJECTS)**

THIS AGREEMENT, made as of this 1<sup>st</sup> day of June, 2011, by and between the OTAY WATER DISTRICT, a municipal water district organized and existing under the laws of the State of California (herein "District") and STRADLING YOCCA CARLSON & RAUTH, a Professional Corporation (herein "Bond Counsel"):

***RECITALS:***

A. The District desires to facilitate the substitution of credit enhancement for and the remarketing of its Otay Water District Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates"); and

B. The District desires to retain Bond Counsel to do the necessary legal work hereinafter outlined, upon the terms and conditions hereinafter set forth, for accomplishing the substitution of credit enhancement for and the remarketing of the Certificates; and

C. Bond Counsel represents that it is ready, willing and able to perform said legal work;

NOW, THEREFORE, in consideration of the premises, and the mutual covenants, terms and conditions herein contained, the parties agree as follows:

1. SCOPE OF SERVICES

A. BOND COUNSEL SERVICES

The District retains Bond Counsel to provide, and Bond Counsel agrees to provide, legal services in connection with the substitution of credit enhancement for and the remarketing of the Certificates. Such services shall include the rendering of a legal opinion pertaining to the Certificates to the effect that the credit substitution is permitted under the Trust Agreement for the Certificates and will not adversely affect the exclusion from gross income for federal income tax purposes of interest due with respect to the Certificates:

Bond Counsel's services will also include:

i. Researching applicable laws and ordinances relating to the substitution of the credit enhancement for and remarketing of the Certificates;

ii. Attending conferences and consulting with District staff and counsel regarding laws applicable to the Certificates, and the need for amendments to any of the existing documentation relating to the Certificates;

iii. Participating in meetings, conferences or discussions with the District's financial advisor, remarketing agent or other experts retained by the District with respect to the substitution of credit enhancement for and the remarketing of the Certificates;

iv. Supervising and preparing documentation of the steps to be taken to accomplish the substitution of credit enhancement for and the remarketing of the Certificates, including:

a. Drafting all resolutions, notices, rules and regulations and other legal documents required for the substitution of credit enhancement for and the remarketing of the Certificates;

b. Preparing the record of proceedings for the authorization of the substitution of credit enhancement for and the remarketing of the Certificates;

c. Assisting in the preparation of the portions of the Reoffering Memorandum for the remarketing of the Certificates which relate to the terms of the Certificates and the firm's legal opinion delivered with respect to the Certificates;

d. Participating in meetings and other conferences scheduled by the District or the District's financial advisor;

e. Consulting with prospective purchasers, their legal counsel and rating agencies;

f. Consulting with the District's General Counsel concerning any legislation or litigation which may affect the Certificates or the security for the Certificates; and

g. Consulting with any trustee or fiscal agent for the Certificates and their counsel.

**B. DISCLOSURE COUNSEL SERVICES**

In addition to the services set forth in Section A above, Bond Counsel agrees to review the Reoffering Memorandum relating to the remarketing of the Certificates and to provide a letter addressed to the remarketing agent to the effect that, to the best knowledge of Bond Counsel, the Reoffering Memorandum does not misstate a material fact or omit a material fact required to be stated therein; provided that no view will be expressed with respect to financial or statistical data therein.

**C. SPECIAL SERVICES**

"Special Services" are defined for purposes of this Agreement as services in addition to the services outlined in Sections A and B above. Special Services will include, but not be limited to, any work after the remarketing of the Certificates related to amendments to the financing documents or agreements and special studies or analyses. Special Services must be authorized in writing by the District's General Manager, Chief Financial Officer or their respective designee.

## 2. COMPENSATION

The District agrees to pay Bond Counsel the following amounts as compensation for services rendered by Bond Counsel under this Agreement:

For the services to be rendered under Section 1.A and B above, Bond Counsel will be paid \$50,000. The fee shall be payable on the date that the Certificates are remarketed and payment is contingent on the remarketing of the Certificates.

A. For performing Special Services as set forth in Section 1.C above, Bond Counsel will be paid fees at the hourly rates set forth in Exhibit A, or in such other manner as is mutually acceptable to the District and Bond Counsel. Such fees will be billed monthly and shall be payable within thirty (30) days following the receipt of each invoice; provided, however, that fees incurred for Special Services prior to the closing date of the Certificates shall, to the extent available, be paid out of the proceeds of the Certificates.

B. In addition to the fees set forth in paragraphs A and B above, Bond Counsel shall be reimbursed for the actual cost of any out-of-pocket expenses reasonably incurred by Bond Counsel in the course of its employment, such as document reproduction, telecommunications charges, printing costs, filing fees, long-distance telephone calls, messenger services, overnight delivery services, travel and similar items of expense. All expenses incurred in connection with services rendered will be billed upon the execution and delivery of the series of the Certificates to which they relate, and may include an estimate of costs to be incurred subsequent to the issuance date.

## 3. PERSONNEL AND CONTRACT ADMINISTRATION

District agrees to accept and Bond Counsel agrees to provide the aforementioned services primarily through Robert J. Whalen, Brian Forbath and Carol L. Lew. If any one of the above attorneys is unable to provide such services due to death, disability or similar event, Bond Counsel reserves the right to substitute another of its attorneys, upon approval by the General Manager, the Chief Financial Officer, or their respective designee, to provide such services; and such substitution shall not alter or affect in any way Bond Counsel's or the District's other obligations under this Agreement.

This Agreement will be administered by the General Manager, the Chief Financial Officer, or their respective designee.

## 4. CONFLICTS OF INTEREST

Bond Counsel represents J.P. Morgan on other matters unrelated to the Certificates. The District hereby provides its informed written consent to Bond Counsel's representation of J.P. Morgan on matters unrelated to the Certificates.

## 5. TERMINATION

A. This Agreement may be terminated without cause by the District or Bond Counsel upon thirty (30) days' advance written notice to the other party. Such notification shall state the effective date of the termination of this Agreement.

B. Bond Counsel reserves the absolute right to withdraw from representing the District if, among other things, the District fails to honor the terms of this Agreement, the District fails to cooperate fully or follow Bond Counsel's advice on a material matter, or any fact or circumstance occurs that would, in Bond Counsel's view, render its continuing representation unlawful or unethical. If Bond Counsel elects to withdraw, the District will take all steps necessary to free Bond Counsel of any obligation to perform further services, including the execution of any documents necessary to complete such withdrawal, and Bond Counsel will be entitled to be paid at the time of withdrawal for all services rendered and costs and expenses paid or incurred on the District's behalf in accordance with the payment terms set forth in Section 2 above. If necessary in connection with litigation, Bond Counsel would request leave of court to withdraw.

C. Bond Counsel's representation of the District will be considered terminated at the earlier of (i) the District's termination of its representation, (ii) Bond Counsel's withdrawal from its representation of the District, or (iii) the substantial completion by Bond Counsel of its substantive work for the District. Unless Bond Counsel has been specifically engaged to perform Special Services related to the Certificates after their remarketing, Bond Counsel's representation of District as to the Certificates shall terminate on the date of remarketing of the Certificates.

## 6. ARBITRATION

IN THE EVENT OF A DISPUTE REGARDING FEES, COSTS, OR ANY OTHER MATTER ARISING OUT OF OR RELATED IN ANY WAY WHATSOEVER TO BOND COUNSEL'S RELATIONSHIP WITH THE DISTRICT, OR BOND COUNSEL'S OR THE DISTRICT'S PERFORMANCE OF THIS AGREEMENT, INCLUDING THE QUALITY OF THE SERVICES WHICH BOND COUNSEL RENDERS, THE DISPUTE SHALL BE DETERMINED, SETTLED AND RESOLVED BY CONFIDENTIAL ARBITRATION IN THE COUNTY OF SAN DIEGO, CALIFORNIA. ANY AWARD SHALL BE FINAL, BINDING AND CONCLUSIVE UPON THE PARTIES, AND A JUDGMENT RENDERED THEREON MAY BE ENTERED IN ANY COURT HAVING JURISDICTION THEREOF. SHOULD YOU ELECT TO HAVE ANY FEE DISPUTE ARBITRATED PURSUANT TO NONBINDING ARBITRATION UNDER STATUTORY OR CASE LAW, THEN SUCH NONBINDING ARBITRATION SHALL DETERMINE ONLY THE ISSUE OF THE AMOUNT OF FEES PROPERLY CHARGEABLE TO YOU. ANY OTHER CLAIMS OR DISPUTES BETWEEN US, INCLUDING CLAIMS FOR PROFESSIONAL NEGLIGENCE, SHALL REMAIN SUBJECT TO BINDING ARBITRATION PURSUANT TO THIS AGREEMENT.

Arbitration may be demanded by the sending of written notice to the other party. If arbitration is demanded, within 20 days of the demand the District shall present a list of five qualified individuals who would be willing to serve that the District would find acceptable to act as arbitrator. To serve as arbitrator, the individual must be a retired judge having served on any federal court or the California Superior Court or higher court in the State of California. Within 20 days of receiving the District's list, Bond Counsel may at its sole discretion (i) select any individual from that list and that individual shall serve as the arbitrator, or (ii) propose its own list of five individuals for arbitrator. If Bond Counsel chooses to present a separate list, the District may within 20 days select any individual from that list and that person shall serve as an arbitrator. If no arbitrator can be agreed upon at the end of this process, the District and Bond Counsel each shall select one individual from its own list and those two persons shall jointly select the arbitrator. The arbitration shall be conducted pursuant to the procedures set forth in the California Code of Civil Procedure §§ 1280 et seq., and in that connection you and we agree that § 1283.05 thereof is applicable to any such arbitration. Nothing

herein shall limit the right of the parties to stipulate and agree to conduct the arbitration pursuant to the then-current rules of the American Arbitration Association, the Judicial Arbitration & Mediation Services, or any other agreed-upon arbitration services provider.

7. MISCELLANEOUS

A. Bond Counsel and the employees of Bond Counsel, in performance of the Agreement, shall act in an independent capacity and not as officers or agents of the District.

B. Without the written consent of the District, this Agreement is not assignable by Bond Counsel in whole or in part.

C. No alteration or variation of the terms of this Agreement shall be valid unless in writing and signed by the parties hereto, and no oral understanding or agreement not incorporated herein shall be binding on any of the parties hereto.

D. In accordance with the requirements of California Business and Professions Code § 6148, Bond Counsel advises you that the firm maintains professional errors and omissions insurance coverage applicable to the services to be rendered to the District.

OTAY WATER DISTRICT

By: \_\_\_\_\_  
General Manager

STRADLING YOCCA CARLSON & RAUTH  
a Professional Corporation

By: \_\_\_\_\_  
Robert J. Whalen

## EXHIBIT A

Shareholders	\$525
Associates	\$295
Paralegals	\$120



STAFF REPORT

TYPE MEETING:	Otay Service Corporation Board Meeting	MEETING DATE:	June 1, 2011
SUBMITTED BY:	Joseph R. Beachem, Chief Financial Officer	W.O./G.F. NO:	DIV. NO.
APPROVED BY: (Chief)			
APPROVED BY: (Asst. GM):	German Alvarez, Administration	Assistant General Manager, Finance and	
SUBJECT:	Substitution of the Letter of Credit for the Outstanding Variable Rate Debt		

GENERAL MANAGER'S RECOMMENDATION:

That the Board of the Corporation adopts Resolution No. 1006 approving the form of documents required for a substitution of the Letter of Credit (LOC) for the outstanding variable rate debt and authorizing the Chief Financial Officer to execute the documents.

COMMITTEE ACTION: \_\_\_\_\_

See Attachment A.

PURPOSE:

To obtain approval by the Board and the Board of Directors of the Otay Service Corporation to amend the Installment Sale Agreement for the 1996 Variable Rate Demand Certificates of Participation, and authorize distribution of a Reoffering Memorandum relating to the substitution of the letter of credit.

ANALYSIS:

SUMMARY

The District's 1996 Variable Rate Demand Certificates of Participation (1996 COPs) are secured by a letter of credit issued by Heleba Landesbank Hessen-Thuringen Girozentrale (Helaba), which was scheduled to expire on June 10, 2011. Staff has obtained a replacement letter of credit from Union Bank, N.A., through a competitive bid process as well as a 30-day

extension of the existing letter of credit to provide for an orderly substitution on or about June 30, 2011.

The 1996 COPs pay interest at a 7-day variable rate and are subject to tender on a weekly basis. A letter of credit (LOC) is required for the 1996 COPs to provide liquidity in the event of such tender, as well as credit support for the issue.

The District's continued Capital Improvement Program requires the ongoing financial funding provided by this debt while the variable rate accomplishes this at a very low cost.

The General Manager has secured the services of Suzanne Harrell, Harrell & Company Advisors, LLC as the Financial Advisor and the legal firm of Stradling, Yocca, Carlson & Rauth to serve as Bond Counsel. Both of these firms were selected due to their excellent work in the past, reasonable fees, and familiarity of the District. Due to these factors, the work can be completed in the short turnaround time required.

Certain documents are required in connection with the substitution of the letter of credit, including a Reimbursement Agreement with Union Bank and a Reoffering Memorandum describing the security for the 1996 COPs for the remarketing of the 1996 COPs on June 30, 2011. The resolutions presented to the District and the Corporation provide for approval of these documents, approval to amend the existing Installment Sale Agreement and to authorize execution of the documents.

#### BACKGROUND

The District currently has five series of outstanding debt and one loan from the State of California. Four of the debt issuances are a fixed rate, and only the 1996 COPs bear interest at a variable rate.

The 1996 COPs are issued in the par amount of \$15,400,000, of which \$11,300,000 is currently outstanding and matures in 2026. The debt was sold by the District to finance the cost of design, acquisition, and construction of certain capital improvements. The debt has a LOC for both credit enhancement and liquidity guarantee provided by Helaba. The LOC allows the interest cost to float at a variable rate, based on a short-term seven-day rate.

Recently, Heleba indicated that they are no longer interested in providing LOCs for debt of the size of the outstanding 1996 COPs

as well as a desire to reduce their exposure to California debt in general. As a result, they have opted to discontinue their services as the LOC Bank. Staff has obtained a replacement letter of credit from Union Bank, N.A., through a competitive bid process as well as a 30-day extension of the Heleba letter of credit to provide for an orderly substitution on or about June 30, 2011.

Substitutions of LOC's are a common occurrence and should raise no concerns. This is a simple substitution with no substantive changes in the debt (the 1996 COPs will have the same maturity and repayment schedule). The most significant change is that Union Bank has a single "A" rating whereas Heleba had a AA rating. Staff did not receive any proposals from banks with AA ratings. This was due to the size of the issue as well as the limited number of AA banks.

The new LOC will enable the 1996 COPs to remain as variable rate debt. This action is consistent with the strategic goal to provide for sound financing of District facilities.

#### OPTIONS

When the Heleba Letter of Credit expires, instead of substituting the LOC and allowing the debt to remain outstanding, the District could consider using its existing reserves to payoff this debt. However, the District's reserves would then fall below the target levels and even below the minimum levels outlined in the Reserve Policy. This would put the District in the position of borrowing other funds at a higher cost.

With the termination of the existing LOC, the District could exercise an option to convert the debt to a fixed rate. Staff, with the assistance of Suzanne Harrell, have determined that the variable rate debt remains financially beneficial to the District. Over the remaining life of the debt, the District is expected to save approximately \$700,000 dollars by retaining the variable rate as compared to a fixed rate, taking in the cost of the LOC substitution. This analysis is required by District's debt policy relating to any conversion of variable rate debt to fixed rate debt. The variable rate debt is approximately 10% of the District's total debt portfolio, and therefore, the District's exposure to fluctuation in interest rates is minimal and manageable.

Maintaining this variable rate debt will also enhance the flexibility of the District to pay down debt as this debt can be prepaid on 30 days notice with no premium. However, based on the District's six-year rate model, the District will need to retain the debt for at least the next six years.

PARTIES AND COSTS

Unlike a new debt issuance, where all costs to establish the debt are paid from the proceeds of the debt issuance, on this substitution the costs will be paid from the District's reserves. The following parties are key in order to complete the LOC substitution. The list below shows the various parties and the related costs.

LOC Bank	100 basis points per year, and \$5,000 closing costs
LOC Bank Counsel	\$40,000
Financial Advisor	\$25,000 paid only if transaction is completed
Bond Counsel	\$40,000 paid only if transaction is completed, and \$2,500 closing costs
Disclosure Counsel	\$10,000 for 10(b)5 opinion required by Remarketing Agent paid only if transaction is completed
Rating Agency	\$5,000

The Financial Advisor, the Bond Counsel, and the Disclosure Counsel were selected under the General Manager's authority based on their prior work with the District and the reasonableness of their fees. This matter is time sensitive so their availability and ability to start working on this project on such short notice was a tremendous benefit to the District.

The rating agency fees are estimated above and are in line with other similar transactions.

The LOC Bank Counsel fees and the LOC Bank fee were competitively bid and were a part of the Union Bank proposal.

FISCAL IMPACT:



The one-time costs to substitute the LOC are expected to be approximately \$127,500. The annual LOC costs are not expected to be significantly different from the existing LOC, and will be approximately \$110,000 per year. The net result of maintaining this variable rate debt as compared to a fixed rate borrowing is

expected to save the District, after the one-time costs, approximately \$700,000 over the next fifteen years - most of which is realized during the next seven years.

**STRATEGIC GOAL:**

Sound financing of District facilities.

**LEGAL IMPACT:** \_\_\_\_\_

None.

  
\_\_\_\_\_  
**General Manager**

Attachments:

- A) Committee Action Form
- B) Resolution No. 1006
- C) Reoffering Memorandum
- D) First Amendment to Installment Sale Agreement



## ATTACHMENT A

<b>SUBJECT/PROJECT:</b>	Substitution of the Letter of Credit for the Outstanding Variable Rate Debt
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### COMMITTEE ACTION:

The Finance, Administration and Communications Committee discussed this item at a meeting held on April 21, 2011 and the following comments were made:

- The District has five (5) outstanding debt issuances that total about \$120 million. The debt is used to fund the District's CIP Program. One (1) of the issuances is a variable rate debt which is a very low cost debt for the District and thus, the District would like to maintain it.
- It was discussed in order for the variable rate debt to be on the market, it gets remarketed every week with a new rate and the structure of the debt requires that another bank step in with a Letter of Credit (LOC) to guarantee the funds to the buyer. Without the LOC, the debt cannot be on the market.
- The current LOC is provided by Helaba and has been in place for 15 years. Helaba has indicated in the past that they are looking to limit their exposure to California debt and that the size of the District's debt is smaller than they wish to work with.
- Staff received notice from Helaba two (2) weeks ago that they will be opting out. Since receiving this notification, staff has engaged, under the General Manager's Authority, Ms. Suzanne Harrell's and a bond counsel's services. They were selected as their fees are reasonable and they have a wealth of experience with the District. The selected bond counsel worked with the District on its last two issuances and was also available to assist with short notice.
- The replacement of LOC's is fairly common and staff, knowing that Helaba may opt out, made contact with a number of banks to assure the District had options.

- An RFP was forwarded to six (6) banks and it is expected that staff will present a recommendation to the board at the May 16 Special Board meeting along with the required resolutions for both the Otay Water District and the Otay Service Corporation to adopt in order to acquire a replacement LOC for the variable debt issuance.
- Ms. Harrell indicated that the variable debt (Certificates of Participation) was issued by the District in 1996 and was secured by installment payments by the Otay Water District to the Otay Service Corporation. The agreement relates to both Otay Water District and the Otay Service Corporation and is the reason both bodies must take action.
- The District and the Otay Service Corporation will also be asked to approve the form of the Reimbursement Agreement which will delineate how the bank, providing the LOC, will be reimbursed if there is ever a draw on the LOC.
- It was noted that there will be a minor modification to the existing Trust Agreement to which the original certificates were issued to conform with the terms of the new Reimbursement Agreement. The Installment Sale Agreement will also be modified to include more contemporary language to match the 2004, 2007 and 2010 issuances.
- Staff will be requesting that the Board authorize the General Manager of the District and the Chief Financial Officer of the Service Corporation to execute all the necessary documents associated to acquire the replacement LOC.
- The RFP deadline is Monday, April 25. On April 26 the District will review the proposals received and make a selection. It was noted that the banks who were forwarded the RFP are 'AA' and 'A' credit banks. The current bank is an 'AA' credit bank. An 'A' credit bank will require that the District pay a little more interest, however, the District will look at the overall cost of the various options and select the option that would provide the least cost.
- It was discussed that the District could convert the debt to a fixed rate debt. However, after evaluating doing so, staff determined that it is still less expensive to keep it

a variable rate debt. Also, in six or seven years, the District may be in a position to pay some debt off. At that time, this variable rate debt can easily be paid off or down. It was further discussed that the variable rate debt is a small portion of the debt portfolio, so any volatility in interest rates would not have a dramatic effect on net portfolio interest expense. Staff also, per policy, reviews the District's outstanding debt periodically to determine if it would be cost effective to convert the debt to a fixed rate, pay it off, etc. The current interest rate on the variable debt is approximately 1.5%. The rate on new fixed rate debts would be approximately 5%.

The committee supported staffs' recommendation and suggested that staff present this item at the May 16, 2011 Special Board Meeting. However, the bond documents were not finalized by the May 16 board meeting and, Helaba had provided a 30-day extension on the LOC, which allowed staff to move the presentation of this item to the June 1, 2011 regularly scheduled meeting.

## RESOLUTION NO. 1006

## RESOLUTION OF THE BOARD OF DIRECTORS OF THE OTAY SERVICE CORPORATION APPROVING CERTAIN DOCUMENTS AND AUTHORIZING CERTAIN ACTIONS IN CONNECTION WITH A CREDIT SUBSTITUTION AND REMARKETING OF THE OTAY WATER DISTRICT VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION (1996 CAPITAL PROJECTS)

WHEREAS, the Otay Water District (the "District") and the Otay Service Corporation (the "Corporation") have previously entered into an Installment Sale Agreement dated as of June 1, 1996 (the "Installment Sale Agreement") and that certain Trust Agreement dated as of June 1, 1996 (the "Trust Agreement") by and among the District, the Corporation and the Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") pursuant to which the Otay Water District Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates") were executed and delivered; and

WHEREAS, the letter of credit securing the repayment of the Certificates under the Trust Agreement is expiring and will not be renewed; and

WHEREAS, the District desires to cause a substitute letter of credit (the "Letter of Credit") from Union Bank, N.A. (the "Bank") to be delivered to the Trustee to replace the existing letter of credit; and

WHEREAS, the substitution of the Letter of Credit from the Bank will result in a mandatory tender and remarketing of the Certificates under the terms of the Trust Agreement; and

WHEREAS, in order to effectuate the substitution of the Letter of Credit to be provided by the Bank and the remarketing of the Certificates, there has been presented to the Corporation the forms of the following documents for approval:

- (1) A Preliminary Reoffering Memorandum; and
- (2) A First Amendment to Installment Sale Agreement (the "First Amendment to Installment Sale Agreement") by and between the District and the Corporation; and

WHEREAS, the adoption of this resolution is necessary to effectuate the remarketing of the Certificates which the Board of Directors has determined to be consistent with the stated purposes of the Corporation to assist the District in its financing needs;

NOW, THEREFORE, the Board of Directors of the Otay Service Corporation does hereby RESOLVE, DETERMINE and ORDER as follows:

Section 1. Each of the above recitals is true and correct.

Section 2. The First Amendment to Installment Sale Agreement is hereby approved and each of the President, Vice President, Executive Director, Chief Financial Officer or Assistant Chief Financial Officer and their written designees (the "Authorized Officers"), acting alone, is hereby authorized and directed to execute and deliver the First Amendment to Installment Sale Agreement in the name of and on behalf of the Corporation, in substantially the form now before this meeting, but with such changes, modification, additions and deletions therein as shall be deemed necessary, desirable or appropriate by the Authorized Officer or Authorized Officers executing the Corporation Agreements. Approval of such changes shall be conclusively evidenced by the execution and delivery of the Corporation Agreements by one or more Authorized Officers.

Section 3. The information regarding the Corporation in the Preliminary Reoffering Memorandum presented at this meeting is hereby approved and the Corporation consents to having the Preliminary Reoffering Memorandum used in connection with the remarketing of the Certificates and each of the Authorized Officers, acting alone, is hereby authorized to execute any certificate deeming the information in the Preliminary Reoffering Memorandum and in the final Reoffering Memorandum regarding the Corporation to be true and accurate.

Section 4. The Authorized Officers are hereby authorized and directed, to do any and all things and to execute and deliver any and all documents, including amendments to any of the existing documents and agreements relating to the Certificates, which they may deem necessary or advisable in order to consummate the delivery of the Letter of Credit from the Bank and the remarketing of the Certificates and otherwise to effectuate the purposes of this resolution.

Section 5. This resolution shall take effect upon its adoption.

ADOPTED, SIGNED and APPROVED at a special meeting of the Corporation this 16th day of May, 2011.

\_\_\_\_\_  
President

ATTEST:

\_\_\_\_\_  
Secretary



DRAFT REOFFERING MEMORANDUM AS OF MAY 25, 2011

REOFFERING - NOT A NEW ISSUE - BOOK-ENTRY-ONLYRATING

Standard &amp; Poor's: \_\_\_\_\_

(See "CONCLUDING INFORMATION - Rating on the Certificates" herein)

On June 18, 1996, Rest Best & Krieger LLP, Riverside, California, Special Counsel to the District, delivered their opinion in connection with the execution and delivery of the 1996 Certificates. Such opinion stated that, based upon an analysis of then existing statutes, regulations, rulings and judicial decisions, and assuming, among other matters, compliance with certain covenants and requirements, the interest component of the installment payments made by the District under the Installment Sale Agreement and received by the Certificate Owners was excluded from gross income for federal income tax purposes, was not an item of tax preference for purposes of federal individual or corporate alternative minimum tax, but such interest component may be included in the calculation of corporation alternative minimum taxable income. In the further opinion of Special Counsel, such interest component was exempt from State of California personal income taxes. In connection with the delivery of the Letter of Credit, Special Counsel will deliver their opinion that such delivery of the Letter of Credit will not, in and of itself, result in the inclusion of component of the installment payments in gross income for purposes of federal income taxation. Special Counsel has not taken and does not intend to take any action to update such opinion or to determine if the interest component of the installment payments is presently excluded from gross income for federal income tax purposes or exempt from State of California personal income taxes. See "LEGAL MATTERS - Tax Matters" herein.

SAN DIEGO COUNTYSTATE OF CALIFORNIA

\$11,300,000

**VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION  
(1996 CAPITAL PROJECTS)**

Evidencing Direct, Undivided Fractional Interests In Installment Payments to be Made by the  
**OTAY WATER DISTRICT**  
As Purchase Price for Certain Property Pursuant to an Installment Sale Agreement

Dated: Date of Initial Delivery

CUSIP: 688818AV5

Due: September 1, 2026

*This Reoffering Memorandum amends, supplements and restates the original Official Statement dated June 17, 1996.*

The Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "1996 Certificates") were originally executed and delivered pursuant to a Trust Agreement dated as of June 1, 1996, as amended (the "Trust Agreement") between the Otay Water District (the "District"), the Otay Service Corporation (the "Corporation") and the Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") and are payable from installment payments to be made by the District to the Corporation as payment for certain real property and improvements pursuant to an Installment Sale Agreement, as described herein and from certain funds held under the Trust Agreement and insurance or condemnation awards. The 1996 Certificates were executed and delivered to provide funds for certain storage, transmission and distribution facilities and the District's administrative headquarters.

Payment of the principal and Purchase Price of and interest component with respect to the 1996 Certificates is supported by an irrevocable, direct-pay letter of credit to be issued by Union Bank, N.A.



The Letter of Credit will permit the Trustee to draw up to an amount sufficient to pay: (i) the principal of the 1996 Certificates when due; (ii) the Purchase Price of 1996 Certificates that are purchased pursuant to tenders and that are not remarketed, and (iii) up to 34 days' interest accrued on the 1996 Certificates, all as described more completely in this Reoffering Memorandum. The Letter of Credit becomes effective on June 1, 2011 and expires on June 1, 2014, or on the earlier occurrence of certain events described in this Reoffering Memorandum. See the captions "THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT" and "THE BANK." On the fifth Business Day prior to the expiration or termination of the Letter of Credit, the 1996 Certificates will be subject to mandatory tender for purchase.

On June 30, 2011, the 1996 Certificates will be remarketed in a Weekly Rate and will continue to bear interest at a Weekly Rate unless and until the Interest Rate Period for the 1996 Certificates is converted to a different Interest Rate Period pursuant to the Trust Agreement. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS." While bearing interest in a Weekly Rate Period, interest with respect to the 1996 Certificates is payable on the first Business Day of each calendar month.

The District is required under the Installment Sale Agreement to make payments in each Fiscal Year from Taxes and from Net Revenues of the District's water system (the "Water System") in an amount sufficient to pay the annual principal and interest due with respect to the Certificates, as described herein (see "SOURCES OF PAYMENT FOR THE CERTIFICATES" and "RISK FACTORS" herein).

The 1996 Certificates are subject to optional and mandatory sinking fund prepayments and optional and mandatory tender prior to maturity as described herein. The 1996 Certificates are also subject to purchase on the demand of Owners under certain circumstances, as described in this Reoffering Memorandum. See "THE CERTIFICATES - General," "Prepayment" and "Tender and Purchase of 1996 Certificates" herein.

The 1996 Certificates were initially executed and delivered on June 18, 1996 in denominations of \$100,000 and any integral multiple thereof, and will continue as such while the 1996 Certificates bear interest in a Weekly Rate Period.

The District's obligation to make the Installment Payments is a special obligation of the District payable solely from Taxes and Net Revenues of the Water System. The obligation of the District to make the Installment Payments is an irrevocable obligation of the District payable solely from Taxes and Net Revenues but does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation other than the Taxes. The obligation of the District to make the Installment Payments under the Installment Sale Agreement does not constitute a debt of the District, the Corporation, the State of California or any political subdivision thereof in contravention of any constitutional or statutory debt limitation or restriction.

This Reoffering Memorandum describes the 1996 Certificates only while bearing interest in a Weekly Rate Period. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate with respect to the 1996 Certificates is changed to an Interest Rate Period other than the Weekly Rate Period. Rather, investors should rely upon the offering documents used in connection with any such change in Interest Rate Period.

*This cover page contains certain information for general reference only. It is not intended to be a summary of the security or terms of the 1996 Certificates. Investors are advised to read the entire Reoffering Memorandum to obtain information essential to making an informed investment decision.*

Certain legal matters related to this Reoffering Memorandum will be passed upon by Rest Best & Krieger LLP, Riverside, California, Special Counsel. Certain legal matters will be passed on for the Remarketing Agent by its counsel, \_\_\_\_\_, for the Bank by its counsel, Musick, Peeler, and Garrett, LLP and for the District and the Corporation by their counsel, Stutz, Arisano, Shindoff & Holtz, San Diego, California, and by Stradling Yoeca Carlson & Routh, a Professional Corporation, Newport Beach, California. It is anticipated that the remarketed Certificates, in book-entry form, will be available for delivery through the facilities of The Depository Trust Company in New York, New York on or about June 30, 2011.

The date of the Reoffering Memorandum is \_\_\_\_\_, 2011.

## GENERAL INFORMATION ABOUT THIS REOFFERING MEMORANDUM

***Use of Reoffering Memorandum.*** This Reoffering Memorandum is submitted in connection with the offer and sale of the 1996 Certificates referred to herein and may not be reproduced or used, in whole or in part, for any other purpose. This Reoffering Memorandum is not to be construed as a contract with the purchasers of the 1996 Certificates.

***Estimates and Forecasts.*** When used in this Reoffering Memorandum and in any continuing disclosure by the District in any press release and in any oral statement made with the approval of an authorized officer of the District or any other entity described or referenced herein, the words or phrases “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “forecast,” “expect,” “intend” and similar expressions identify “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is subject to such uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material. Such forward-looking statements include, but are not limited to, certain statements contained in the information under the caption “THE WATER SYSTEM.”

***Limit of Offering.*** No dealer, broker, salesperson or other person has been authorized by the District to give any information or to make any representations in connection with the offer or sale of the Certificates other than those contained herein and if given or made, such other information or representation must not be relied upon as having been authorized by the District or the Remarketing Agent. This Reoffering Memorandum does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the 1996 Certificates by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

***Involvement of Remarketing Agent.*** The Remarketing Agent has provided the following sentence for inclusion in this Reoffering Memorandum: The Remarketing Agent has reviewed the information in this Reoffering Memorandum in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Remarketing Agent does not guarantee the accuracy or completeness of such information.

***Information Subject to Change.*** The information and expressions of opinions herein are subject to change without notice and neither delivery of this Reoffering Memorandum nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District or any other entity described or referenced herein since the date hereof. All summaries of the documents referred to in this Reoffering Memorandum are made subject to the provisions of such documents, respectively, and do not purport to be complete statements of any or all of such provisions.

THE CERTIFICATES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXCEPTION FROM THE REGISTRATION REQUIREMENTS CONTAINED IN SUCH ACT. THE CERTIFICATES HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE.

The CUSIP number of the 1996 Certificates is provided by Standard & Poor’s CUSIP® Service Bureau and is set forth herein for convenience of reference only. Neither the District nor the Remarketing Agent takes any responsibility for the accuracy of such number.

**OTAY WATER DISTRICT  
SAN DIEGO COUNTY, CALIFORNIA**

**BOARD OF DIRECTORS**

Jaime Bonilla, *President - Division 2*  
Gary D. Croucher, *Vice President - Division 3*  
David Gonzalez, Jr., *Treasurer - Division 1*  
Jose Lopez, *Division 4*  
Mark Robak, *Division 5*

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**MANAGEMENT TEAM**

Mark Watton, *General Manager*  
German Alvarez, *Assistant General Manager Finance & Administration*  
Manny Magaña, *Assistant General Manager Engineering & Operations*  
Joseph R. Beachem, *Chief Financial Officer*  
Rom Sarno, Jr., *Chief of Administrative Services*  
Geoff Stevens, *Chief Information Officer*  
Rod Posada, *Chief of Engineering*  
Pedro Porras, *Chief of Water Operations*

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**PROFESSIONAL SERVICES**

**Special Counsel**

Best Best & Krieger LLP  
Riverside, California

**General Counsel to the District**

Stutz, Artiano, Shinoff & Holtz  
San Diego, California

**Remarketing Agent**

J.P. Morgan Securities LLC  
New York, New York

**Trustee, Tender Agent and Paying Agent**

The Bank of New York Mellon Trust Company, N.A.  
Los Angeles, California

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# REOFFERING MEMORANDUM

\$11,300,000

## VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION (1996 CAPITAL PROJECTS)

Evidencing Direct, Undivided Fractional Interests in Installment Payments to be Made by the  
OTAY WATER DISTRICT  
As Purchase Price for Certain Property Pursuant to an Installment Sale Agreement

## INTRODUCTION

*This Reoffering Memorandum dated June \_\_, 2011 amends, supplements and restates the original Official Statement dated June 17, 1996, with respect to the Variable Rate Demand Certificates of Participation (1996 Capital Projects) of the Otay Water District (the "1996 Certificates").*

*The 1996 Certificates were originally executed and delivered on June 18, 1996 in the original principal amount of \$15,400,000, of which \$11,300,000 remains outstanding.*

*This Introduction is subject in all respects to the more complete information contained and referenced elsewhere in this Reoffering Memorandum. The offering of the 1996 Certificates to potential investors is made only by means of the entire Reoffering Memorandum.*

### **Purpose**

The purpose of this Reoffering Memorandum, which includes the cover page and appendices hereto, is to set forth certain information concerning the Otay Water District, located in San Diego County, California (the "District"), in connection with \$15,400,000 aggregate principal amount of the 1996 Certificates. The 1996 Certificates evidence direct, undivided fractional interests of the registered owners thereof in Installment Payments to be made by the District, as payment for certain property pursuant to an Installment Sale Agreement dated as of June 1, 1996, as amended (the "Installment Sale Agreement") with the Otay Service Corporation (the "Corporation"). The 1996 Certificates were executed and delivered for the purposes of financing certain capital improvements of the District, and paying the costs of issuance of the 1996 Certificates. Capitalized terms used herein and not otherwise defined have the meanings ascribed to them in "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

### **The District**

The District was established in 1956. The District is a municipal water district organized and existing under and in accordance with Division 20 of the Water Code of the State of California, commencing with Section 71000, as amended (the "Law"). The District's boundaries currently encompass an area of approximately 125 square miles in San Diego County, lying immediately east of the San Diego metropolitan area and running from the City of El Cajon south to the Mexican border, abutting the cities of El Cajon and La Mesa and encompassing most of the City of Chula Vista and a small portion of the City of San Diego. The District currently serves a population of approximately 206,000 and expects the service area to experience moderate growth in the next ten years (see "OTAY WATER DISTRICT" and "APPENDIX C - ECONOMIC PROFILE FOR THE COUNTY OF SAN DIEGO" herein).

## **The Corporation**

The Corporation was organized pursuant to the Nonprofit Public Benefit Corporation Law of the State of California, being Part 2 of Division 2 of Title 1 of the California Corporations Code. It was formed for the purpose of providing financial assistance to the District by acquiring, constructing, improving and developing certain real and personal property, together with appurtenances and appurtenant work for the use, benefit and enjoyment of the public. The District's Board of Directors sits as the Corporation's Board of Directors.

## **The 1996 Certificates**

The 1996 Certificates will bear interest at the Weekly Rate, which will be computed on the basis of a year of 365 days (366 days in leap years) and the actual days elapsed and will accrue from and including the first day of each calendar month through the last day of such month (except that the initial interest period will commence on June 30, 2011). Such interest will be paid on the first Business Day of the following month, commencing August 1, 2011. When the 1996 Certificates bear interest at a Weekly Rate, interest will be determined as described under the caption "THE CERTIFICATES - Interest Rates - Weekly Rate."

The method of determining the interest rate borne by the 1996 Certificates may be changed at the option of the District in accordance with the terms of the Trust Agreement, upon notice to the Owners of the 1996 Certificates, to a Daily Rate, a Weekly Rate, a Monthly Rate, a CP Rate, or a Fixed Rate. See the caption "THE CERTIFICATES - Interest Rates."

**This Reoffering Memorandum describes the 1996 Certificates only while bearing interest at a Weekly Rate. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate period on the 1996 Certificates is changed to a period other than the Weekly Rate Period. Rather, investors should rely upon the offering document used in connection with any such change in Interest Rate Period.**

## **Security for the 1996 Certificates**

The 1996 Certificates were originally executed and delivered as variable rate certificates bearing interest in a Weekly Rate Period on June 18, 1996. On June 30, 2011 (the "Reoffering Date"), the 1996 Certificates will be remarketed in a Weekly Rate Period supported by an irrevocable direct-pay letter of credit to be issued by Union Bank, N.A. (the "Bank"). See "THE LETTER OF CREDIT AND REIMBURSEMENT AGREEMENT" herein. The 1996 Certificates presently and will continue to bear interest at a Weekly Rate unless and until the Interest Rate Period for the 1996 Certificates is converted to a different Interest Rate Period pursuant to the Trust Agreement.

The 1996 Certificates represent undivided fractional interests in the Installment Payments (the "Installment Payments") to be made by the District to the Corporation as the payment for the 1996 Project, as described herein, pursuant to a Installment Sale Agreement, dated as of June 1, 1996, between the Corporation and the District, as amended by a First Supplement to Installment Sale Agreement dated as of June 1, 2011 (as amended the "Installment Sale Agreement"). The Installment Payments are scheduled to be sufficient to pay, when due, the annual principal and interest represented by the Certificates. The Corporation has assigned to the Trustee, for the benefit of the Owners of the 1996 Certificates, the right of the Corporation to receive and collect the Installment Payments due from the District to the Corporation under the Installment Sale Agreement and other amounts payable by the District to the Corporation thereunder. For a summary of the Trust Agreement, the Installment Sale Agreement and the Reimbursement Agreement see "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS" herein. Certain capitalized terms used in this Reoffering Memorandum and not otherwise defined have the meaning given them in "APPENDIX A."

The Installment Payments are secured by a charge and lien on Taxes and Revenues of the Water System and are payable from Taxes and Net Revenues, on a parity with:

- the payments required to be made by the District under an installment purchase agreement dated as of July 1, 2004 (the “2004 Installment Purchase Agreement”) securing the District’s outstanding Revenue Refunding Certificates of Participation (1993 Water Facilities Project), Series 2004 (the “2004 Certificates”),
- the payments required to be made by the District under an installment purchase agreement dated as of March 1, 2007 (the “2007 Installment Purchase Agreement”) securing the District’s outstanding Revenue Certificates of Participation (2007 Water System Project), Series 2007 (the “2007 Certificates”), and
- the payments required to be made by the District under an installment purchase agreement dated as of March 1, 2010 (the “2010 Installment Purchase Agreement”) securing the Otay Water District Financing Authority’s outstanding Water Revenue Bonds, Series 2010A and Water Revenue Bonds, Series 2010B (collectively, the “2010 Bonds”).

See “SOURCES OF PAYMENT FOR THE CERTIFICATES - Installment Payments” herein.

Collectively, the 2004 Certificates, the 2007 Certificates and the 2010 Bonds are referred to herein as the “Existing Parity Obligations.” See “THE WATER SYSTEM - Outstanding Indebtedness of the District” herein.

**The District’s obligation to make the Installment Payments is a special obligation of the District payable solely from Taxes and Net Revenues of the Water System. The obligation of the District to make the Installment Payments is an irrevocable obligation of the District payable solely from Taxes and Net Revenues but does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation other than the Taxes. The obligation of the District to make the Installment Payments under the Installment Sale Agreement does not constitute a debt of the District, the Corporation, the State of California or any political subdivision thereof in contravention of any constitutional or statutory debt limitation or restriction.**

## **Letter of Credit**

On June 30, 2011, an irrevocable direct-pay letter of credit, dated June 30, 2011 (the “Letter of Credit”), provided by Union Bank, N.A. (the “Bank”), is expected to replace the existing irrevocable, direct-pay letter of credit issued by Heleba Landesbank Hessen-Thüringen Girozentrale, to support the payment of the principal and Purchase Price of, and interest on, the 1996 Certificates. The Letter of Credit will be issued pursuant to a Reimbursement Agreement, dated as of June 30, 2011 (the “Reimbursement Agreement”), to be entered into by and between the District and the Bank. The Letter of Credit will expire on June \_\_, 2014, or on the earlier occurrence of certain events as described herein. The initial Letter of Credit may be replaced with another credit facility as described under the caption “THE LETTER OF CREDIT AND REIMBURSEMENT AGREEMENT.” The initial Letter of Credit, or any qualified replacement or extension, issued by the Bank, or any other financial institution, is called a “Letter of Credit.” Any financial institution which at the time is the issuer of a Letter of Credit is called the “Bank.”

The initial Letter of Credit will be issued in the total amount of \$11,426,313, which is equal to: (i) the outstanding aggregate principal amount of the 1996 Certificates (\$11,300,000); plus (ii) 34 days’ interest thereon at an annual rate of 12% (\$126,313).

## **No Continuing Disclosure**

The 1996 Certificates are exempt from the rules of the Securities and Exchange Commission relating to continuing disclosure of annual financial information and certain material events. However, the District provides continuing disclosure of annual financial information and certain material events with respect to the Existing Parity Obligations.

## **Information Concerning this Reoffering Memorandum**

This Reoffering Memorandum speaks only as of its date. The information set forth herein has been obtained by the District from sources which are believed to be accurate and complete, but such information is not guaranteed as to accuracy or completeness, nor has it been independently verified and is not to be construed as a representation by the District or the Remarketing Agent. Statements contained in this Reoffering Memorandum which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended as such and are not to be construed as representations of fact.

**Availability of Legal Documents.** The summaries and references contained herein with respect to the Trust Agreement, the Installment Sale Agreement, the Reimbursement Agreement, the Certificates and other statutes or documents do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute, and references to the 1996 Certificates are qualified in their entirety by reference to the form thereof included in the Trust Agreement. Definitions of certain terms used herein are set forth in "APPENDIX A" hereto. Copies of these documents may be obtained at the corporate trust office of the Trustee, The Bank of New York Mellon Trust Company, N.A., Los Angeles, California or from the District, 2554 Sweetwater Springs Blvd., Spring Valley, California 91978.

## **THE CERTIFICATES**

### **General**

**This Reoffering Memorandum describes the 1996 Certificates only while bearing interest at a Weekly Rate. Investors should not rely upon the information in this Reoffering Memorandum in the event that the method of determining the interest rate period on the 1996 Certificates is changed to a period other than the Weekly Rate Period. Rather, investors should rely upon the offering document used in connection with any such change in Interest Rate Period.**

The 1996 Certificates were initially executed and delivered in the aggregate principal amount of \$15,400,000, of which \$11,300,000 remains outstanding. The 1996 Certificates are dated the date of initial delivery of the 1996 Certificates, and will bear interest at a Weekly Rate, until converted to another interest rate Mode as described herein. The 1996 Certificates will mature, subject to prior redemption, on September 1, 2026. Interest with respect to the 1996 Certificates bearing interest at the Weekly Rate accruing during any month will be payable on the first Business Day of the following month. Interest with respect to the 1996 Certificates is also payable on any Mandatory Purchase Date. Interest will be determined as described herein. While bearing interest at the Weekly Rate, the 1996 Certificates will be issued in Authorized Denominations of \$100,000 and any integral multiple thereof.

The term "Business Day" is defined in the Trust Agreement to mean any day of the year other than Saturday or Sunday on which banks in New York, New York, and in Los Angeles, California, or any other city in which the principal office of the Bank may be located are not authorized or required by law or executive order to close and on which the New York Stock Exchange is not closed. If the date for making any payment on the 1996 Certificates is not a Business Day, the payment will be made on the next Business Day with the same effect as if made on the nominal date and no interest will accrue between the nominal date and the actual payment date.

The 1996 Certificates will be registered in the name of Cede & Co., as registered owner and nominee of The Depository Trust Company, New York, New York ("DTC"). So long as DTC, or its nominee Cede & Co., is the registered owner of all the 1996 Certificates, all payments of principal of and interest with respect to the 1996 Certificates and the Purchase Price of the 1996 Certificates will be made directly to DTC. Disbursement of such payments to the DTC Participants (as defined below) will be the responsibility of DTC. Disbursement of such payments to the Beneficial Owners (as defined below) of the 1996 Certificates will be the responsibility of the DTC Participants as more fully described herein. See the caption "Book-Entry Only System" below and "APPENDIX E - DTC AND THE BOOK-ENTRY-ONLY SYSTEM."

*There are a number of provisions in the Trust Agreement relating to the terms of Bank Certificates (i.e., 1996 Certificates purchased by the Bank pursuant to the Letter of Credit and Reimbursement Agreement) that are not described in this Reoffering Memorandum. All references to the terms of the 1996 Certificates in this Reoffering Memorandum describe only 1996 Certificates that are not owned by the Bank unless expressly indicated herein.*

## **Interest Rates**

**General.** The method of determining the interest rate borne by the 1996 Certificates may be changed at the option of the District in accordance with the terms of the Trust Agreement, upon notice to the Owners of the 1996 Certificates, to a Daily Rate, a Weekly Rate, a Monthly Rate (collectively, the "Variable Rates"), a CP Rate, or a Fixed Rate.

The Variable Rate is required to be the lowest rate of interest which, in the judgment of the Remarketing Agent, would cause the 1996 Certificates to have a market value equal to the principal amount thereof, plus accrued interest, under prevailing market conditions as of the date of determination of the Variable Rate. In no event may the Variable Rate for any Variable Rate Period exceed 12% (the "Maximum Rate").

All determinations of Variable Rates pursuant to the Trust Agreement are conclusive and binding upon the District, the Corporation, the Trustee, the Tender Agent, the Bank and the Owners of the 1996 Certificates.

**Weekly Rate.** Commencing June 30, 2011, the 1996 Certificates will bear interest at the Weekly Rate, which will be computed on the basis of a year of 365 days (366 days in leap years) and the actual days elapsed and will accrue from and including the first day of each calendar month through the last day of such month (except that the initial interest period will commence on June 30, 2011). Such interest will be paid on the first Business Day of the following month, commencing August 1, 2011.

The Weekly Rate for each Weekly Rate Period is required to be determined by the Remarketing Agent not later than 4:30 p.m. (New York City time) on each Tuesday or, if such Tuesday is not a Business Day, the last Business Day immediately prior to the commencement date of the Weekly Rate Period to which it relates. Weekly Rate Periods extend from Wednesday of each week to but excluding Wednesday of the following week except that in the case of a conversion to a Weekly Rate Period from a different Variable Rate Period or from CP Rate Periods, the initial Weekly Rate Period for the 1996 Certificates will extend from the Weekly Rate Conversion Date to Wednesday of the following week; in the case of a conversion of 1996 Certificates from a Weekly Rate Period to a different Rate Period, the last Weekly Rate Period will end on the Conversion Date; and, in the case of the first Weekly Rate Period, which shall commence on the Date of Delivery of the 1996 Certificates and extend to Wednesday of the following week.

## **Conversion Between Variable Rate Periods and CP Rate Periods**

At the option of the District, subject to certain conditions, and upon proper notice to the Trustee, the 1996 Certificates may be converted from one Variable Rate Period to another Variable Rate Period or to or from CP Rate Periods in accordance with the provisions therefor in the Trust Agreement.

Upon a conversion of 1996 Certificates to or from one Variable Rate Period to another Variable Rate Period or to or from CP Rate Periods, such 1996 Certificates will be subject to a mandatory tender, and the Owners of such 1996 Certificates may not elect to retain their 1996 Certificates.

In the case of conversion between Variable Rate Periods or to CP Rate Periods, the Conversion Date is required to be an Interest Payment Date for the Variable Rate Period from which the conversion is to be made. In the case of conversion from CP Rate Periods, the Conversion Date is required to be both (1) the first Business Day of a calendar month and (2) the last Interest Payment Date on which interest is payable for any CP Rate Periods previously established for any 1996 Certificate pursuant to the Trust Agreement.

Not less than 30 days nor more than 60 days prior to the Conversion Date, the Trustee is required to mail or cause the Trustee to mail a written notice of the conversion to the Bank, the District and all of the Owners of the 1996 Certificates.

Notwithstanding the delivery of notice of conversion pursuant to the Trust Agreement conversion to a new Rate Period will not take effect if:

- (1) The Remarketing Agent fails to determine a Variable Rate or CP Rate for the Rate Period to which the conversion is to be made;
- (2) Any notice of conversion required by the Trust Agreement is not given when required;
- (3) There is not delivered to the District, the Remarketing Agent and the Trustee an Opinion of Special Counsel dated as of the Conversion Date; or
- (4) Such notice of conversion is rescinded by the District by written notice to the Trustee and the Remarketing Agent delivered prior to the applicable Conversion Date. If the Trustee receives notice of such rescission prior to the time the Trustee has given notice to the Owners of the 1996 Certificates, then such notice of conversion will be of no force and effect. If the Trustee receives notice of such rescission after the Trustee has given notice to the Owners of the 1996 Certificates, then the Certificates will automatically adjust to the Weekly Rate Period. Any purchases of 1996 Certificates scheduled or required to take place on the proposed effective date of any Rate Period will take place on such date. Any election to retain 1996 Certificates which are subject to mandatory tender, received by the Trustee pursuant to the Trust Agreement will be of no force and effect and the Trustee will immediately give written notice thereof to such Owners. No Opinion of Special Counsel is required in connection with any automatic adjustment to a Weekly Rate Period pursuant to such provision in the Trust Agreement.

Except as provided in (4) above, in any such event, the 1996 Certificates which were to be converted will automatically be converted to a Weekly Rate Period on the date such conversion was to be made, but any mandatory or optional tender for purchase on the Conversion Date will be carried out. No cancellation of a conversion will constitute an Event of Default under the Trust Agreement. Upon the occurrence of any event described in (1) above, the Weekly Rate will be the per annum rate of interest determined on each Tuesday (or if such day is not a Business Day, the next prior Business Day) by the Trustee which is 80% of the certificate equivalent yield for 30-day United States Treasury Bills sold at the last United States Treasury auction occurring prior to such day, which yield shall be calculated in accordance with standard practices in the banking industry on the basis of the discount rates at which such bills were sold but not to exceed the Maximum Rate.

## **Conversion to Fixed Rates**

The 1996 Certificates, in whole but not in part, will be converted to represent interest calculated at Fixed Rates upon the District's request. Upon a conversion of 1996 Certificates to represent interest calculated at Fixed Rates, such 1996 Certificates will be subject to mandatory tender, and the Owners of such 1996 Certificates may not elect to retain their 1996 Certificates. As a condition of any Fixed Rate conversion, the Trustee, the Bank and the Remarketing Agent must receive an Opinion of Special Counsel. The Fixed Rate Conversion Date will be (1) in the case of a conversion from a Variable Rate Period, an Interest Payment Date for the 1996 Certificates for the Variable Rate Period from which the conversion is to be made, and (2) in the case of a conversion from CP Rate Periods, a day which is both (A) the first Business Day of a calendar month and (B) the last Interest Payment Date for the 1996 Certificates on which interest is payable for any and all CP Rate Periods theretofore established for the 1996 Certificates pursuant to the Trust Agreement.

The Fixed Rate is required to be the lowest rate (not in excess of the maximum rate of interest allowed by law) which, in the judgment of the Remarketing Agent, as of the date of determination and under prevailing market conditions, would cause the 1996 Certificates of such maturities to have a market value equal to the principal amount thereof, plus accrued interest.

The Trustee is required to mail or cause the Trustee to mail a notice of the proposed conversion to the Owners of all 1996 Certificates to be converted not less than 30 days nor more than 60 days prior to the proposed Fixed Rate Conversion Date and state that (1) the 1996 Certificates are subject to mandatory tender for purchase with no right to retain on the Fixed Rate Conversion Date at a Purchase Price of par plus accrued interest; and (2) on and after the Fixed Rate Conversion Date the Certificate's shall be deemed purchased on that date, and thereafter the Owner will have no further rights under the Trust Agreement except to receive the Purchase Price.

Notwithstanding the delivery of notice of a Fixed Rate conversion pursuant to the Trust Agreement, conversion of the 1996 Certificates to a Fixed Rate Period will not take effect if (1) the District withdraws such notice of conversion not later than the Business Day preceding the date on which the Fixed Rate is to be determined; (2) the Remarketing Agent fails to determine a Fixed Rate; (3) any notice required by the Trust Agreement is not given when required; or (4) upon conversion any Fixed Rate 1996 Certificates would be Bank 1996 Certificates unless the Bank consents. In any of such events, the 1996 Certificates will automatically be converted to a Weekly Rate for a Weekly Rate Period which will commence on the date the Fixed Rate conversion was to be made, but the mandatory tender for purchase will still be carried out if notice of the Fixed Rate conversion had been given to the Owners. Withdrawal of a conversion notice must be given by the District to the Trustee, the Tender Agent, the Remarketing Agent and the Bank, by telephone, promptly confirmed in writing. No cancellation of a Fixed Rate conversion pursuant to this paragraph constitutes an Event of Default under the Trust Agreement. If the 1996 Certificates are converted to represent interest calculated at a Weekly Rate rather than a Fixed Rate, and the Remarketing Agent fails to set a Weekly Rate, the Weekly Rate shall be the per annum rate of interest determined on each Tuesday (or if such day is not a Business Day, the immediately preceding Business Day) by the Trustee which is 80% of the certificate equivalent yield for 30-day United States Treasury Bills sold at the last United States Treasury auction occurring prior to such day, which yield shall be calculated in accordance with standard practices in the banking industry on the basis of the discount rate at which such bills were sold but will not exceed the Maximum Rate.

Following the Fixed Rate Conversion Date, the 1996 Certificates will no longer be secured by the Letter of Credit and will no longer be subject to tender for purchase.

## Tender and Purchase of 1996 Certificates

### Tenders During Variable Rate Periods

During any Variable Rate Period with respect to the 1996 Certificates, the Owners of 1996 Certificates (other than Bank 1996 Certificates) may elect to have their 1996 Certificates (or portions thereof in Authorized Denominations) purchased at the Purchase Price as set forth below:

- 1996 Certificates representing interest at Daily Rates may be tendered for purchase on any Business Day upon telephonic notice of tender given (promptly confirmed in writing) to the Tender Agent not later than 11:00 a.m. (New York City time) on the Purchase Date.
- 1996 Certificates representing interest at Weekly Rates may be tendered for purchase on any Business Day upon telephonic notice of tender (promptly confirmed in writing) to the Tender Agent not later than 5:00 p.m. (New York City time) on a Business Day not less than seven days prior to the Purchase Date.
- 1996 Certificates representing interest at Monthly Rates may be tendered for purchase on any Interest Payment Date upon delivery of a written notice of tender to the Tender Agent not later than 4:00 p.m. (New York City time) on a Business Day that is not less than 7 days prior to the Purchase Date.

Each notice of tender must, in the case of a written notice, be delivered to the Tender Agent at the address below, and must be satisfactory to the Tender Agent. Such notice of tender must also state, whether delivered in writing or by telephone, promptly confirmed in writing, the principal amount of the 1996 Certificate or portion thereof, that the Owner irrevocably demands purchase of such 1996 Certificate or portion thereof, the date on which such 1996 Certificate or portion thereof is to be purchased and payment instructions. Such notice of tender will automatically constitute, whether delivered in writing or by telephone, (A) an irrevocable offer to sell the 1996 Certificates (or portion thereof) to which the notice relates on the Purchase Date to any purchaser selected by the Remarketing Agent at the Purchase Price, (B) an irrevocable authorization and instruction to the Trustee to effect transfer of such 1996 Certificates (or portion thereof), upon payment of such price to the Trustee on the Purchase Date, (c) an irrevocable authorization and instruction to the Tender Agent to effect the exchange of the 1996 Certificates to be purchased in whole or in part for other 1996 Certificates in an equal aggregate principal amount so as to facilitate the sale of such 1996 Certificates (or portion thereof), and (D) an acknowledgment that such Owner will have no further rights with respect to such 1996 Certificates (or portion thereof) upon payment of the Purchase Price thereof by the Trustee on the Purchase Date, except for the right of such Owner to receive such Purchase Price upon surrender of such 1996 Certificates to the Tender Agent. The determination of the Tender Agent as to whether a notice of tender has been properly delivered pursuant to the foregoing will be conclusive and binding upon the Owner.

Notices in respect of optional tenders must be delivered to the Tender Agent as follows:

#### First Class/Registered/Certified

The Bank of New York Mellon Trust Company,  
N.A.  
Global Corporate Trust  
P.O. Box 396  
East Syracuse, NY 13057  
Telephone: (800) 254-2826

#### Express Delivery Only

The Bank of New York Mellon Trust Company,  
N.A.  
Global Corporate Trust  
111 Sanders Creek Parkway  
East Syracuse, NY 13057  
Telephone: (800) 254-2826

### **Mandatory Tenders Upon Conversion**

In the case of any conversion from one Variable Rate Period to another Variable Rate Period or to a CP Rate Period, the 1996 Certificates to be converted are subject to mandatory tender for purchase on the Conversion Date at the Purchase Price.

### **Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit**

Prior to the Fixed Rate Conversion Date of the 1996 Certificates, the 1996 Certificates are subject to mandatory tender for purchase without the right to retain at the Purchase Price on a Business Day that is at least five days prior to the date on which the Letter of Credit is to be cancelled in connection with replacement by a Substitute Facility pursuant to the Trust Agreement. The 1996 Certificates are also subject to mandatory tender for purchase without the right to retain at the Purchase Price on a Business Day which is at least five days prior to a termination or expiration of the Letter of Credit. In either event, the Owners of the 1996 Certificates may not elect to retain their 1996 Certificates.

Notice of mandatory tender is required to be given by mail by the Registrar at the direction of the Trustee to the Bank and the Owners of such 1996 Certificates by first class mail not less than 15 nor more than 60 days prior to the mandatory tender date.

### **Purchase of Tendered 1996 Certificates**

Before 4:00 p.m. (New York City time) on the Purchase Date and upon receipt by the Trustee of 100% of the aggregate Purchase Price of the tendered 1996 Certificates, the Trustee is required to pay the Purchase Price of such 1996 Certificates to the Owners thereof at its principal office or by bank wire transfer. Payments are required to be made in immediately available funds. All 1996 Certificates to be purchased on any date are required to be delivered to the principal corporate trust office of the Tender Agent at or before 11:30 a.m. (New York City time) on the Purchase Date.

If the Owner of any 1996 Certificates (or portion thereof) that is subject to purchase pursuant to the Trust Agreement fails to surrender such 1996 Certificates to the Tender Agent for purchase on the Purchase Date, and if the Tender Agent is in receipt of the Purchase Price therefor, such 1996 Certificates (or portion thereof) will nevertheless be deemed purchased on the Purchase Date and ownership of such 1996 Certificates (or portion thereof) will be transferred to the purchaser thereof as provided in the Trust Agreement. Any Owner who fails to deliver a 1996 Certificate for purchase as required above will have no further rights thereunder except the right to receive the Purchase Price thereof upon presentation and surrender of said 1996 Certificate to the Tender Agent.

### **Insufficient Funds for Purchases**

If as a result of a default by the Bank under the terms of the Letter of Credit the moneys available for purchase of 1996 Certificates pursuant to the Trust Agreement are inadequate for the purchase of all 1996 Certificates that are tendered on any Purchase Date, all 1996 Certificates will continue to represent interest at the same rate as in effect on the day prior to the Purchase Date to the date on which the earliest of the following occurs: (i) the Fixed Rate Conversion Date for the 1996 Certificates, (ii) the date on which any default by the Bank under the terms of the Letter of Credit has been cured, or (iii) the date on which a Substitute Facility meeting the requirements of the Trust Agreement has been obtained. If there are insufficient funds for purchase, the Trustee is required immediately (but no later than the end of the next succeeding Business Day) to return all tendered 1996 Certificates to the Owners thereof, return all moneys received from the purchase of such 1996 Certificates to the persons who provided such moneys and notify all Owners of the 1996 Certificates and the Bank in writing of the interest rate to be effective.

## **Tender of 1996 Certificates in Book-Entry System Are Subject to DTC Procedures**

As long as the book-entry system is in effect with respect to the 1996 Certificates, all tenders for purchase and deliveries of 1996 Certificates optionally tendered for purchase upon election of the Owner or subject to mandatory tender under the provisions of the Trust Agreement will be made pursuant to DTC's procedures as in effect from time to time, and none of the District, the Trustee or the Remarketing Agent have any responsibility for or liability with respect to the implementation of such procedures. For a description of the tender procedures through DTC, see "APPENDIX E - DTC AND THE BOOK-ENTRY-ONLY SYSTEM."

## **Prepayment**

### **Optional Prepayment**

While the 1996 Certificates bear interest at a Weekly Interest Rate, the 1996 Certificates are subject to prepayment at the option of the District, in whole or in part on any Interest Payment Date at a prepayment price of 100% of the principal amount thereof.

### **Mandatory Prepayment**

***Mandatory Sinking Fund Prepayment.*** The 1996 Certificates are subject to mandatory sinking fund prepayment on September 1 in each year on or after September 1, 2011 by lot, at a prepayment price equal to the principal amount thereof, without premium, together with accrued interest to the date of prepayment, from the principal component of the Installment Payment to be paid by the District pursuant to the Installment Sale Agreement with respect to each such prepayment date as follows:

<u>Prepayment Date</u> <u>(September 1)</u>	<u>Principal Amount</u> <u>of 1996 Certificates</u> <u>To Be Prepaid</u>
2011	\$ 400,000
2012	500,000
2013	500,000
2014	500,000
2015	600,000
2016	600,000
2017	600,000
2018	700,000
2019	700,000
2020	700,000
2021	800,000
2022	800,000
2023	900,000
2024	900,000
2025	1,000,000
2026 (maturity)	1,100,000

If some but not all of the 1996 Certificates have been otherwise prepaid, the total principal amount of 1996 Certificates to be prepaid pursuant to a mandatory sinking fund prepayment subsequent to such other prepayment shall be reduced to correspond to the principal components of the Installment Payments scheduled to be paid in each year thereafter pursuant to the Installment Sale Agreement. If the sinking

fund prepayment amounts of the final maturity of the 1996 Certificates are converted to serial maturities, then such 1996 Certificates shall not be subject to mandatory sinking fund prepayment.

***Prepayment From Net Proceeds of Insurance and Condemnation.*** The 1996 Certificates are subject to mandatory prepayment on the earliest practicable date for which notice of prepayment may be given, from net proceeds of insurance or condemnation of the 1996 Project (including the proceeds of any self-insurance), as a whole or in part, in any integral multiple of an authorized denomination, at a prepayment price equal to the principal amount thereof, together with accrued interest to the date fixed for prepayment, without premium. Any surplus net proceeds not equal to an authorized denomination shall be deposited in the Principal Account of the Certificate Payment Fund.

### **General Prepayment Provisions**

***Selection of 1996 Certificates for Prepayment.*** The 1996 Certificates shall be prepaid in the following order of priority (and, subject to the foregoing, by lot within each priority):

First, any Bank Certificates;

Second, any 1996 Certificates which have been tendered to the Tender Agent on the date fixed for prepayment, the notice of which tender shall have been given to the Trustee prior to the selection of 1996 Certificates for such prepayment pursuant to the Trust Agreement; and

Third, the Outstanding 1996 Certificates not previously called for prepayment.

***Notice of Prepayment.*** When prepayment is authorized or required pursuant to the Trust Agreement, the Trustee shall give notice of the prepayment of the 1996 Certificates. Such notice shall specify: (a) that the 1996 Certificates or a designated portion thereof are to be prepaid, (b) the date of prepayment, and (c) the place or places where the prepayment will be made. Such notice shall further state that on the specified date there shall become due and payable upon each Certificate, the principal, together with interest accrued to said date, and that from and after such date interest with respect thereto shall cease to, accrue and be payable.

Notice of the prepayment of 1996 Certificates, other than mandatory sinking fund prepayment and excepting any notice that refers to 1996 Certificates that are the subject of an advance refunding, shall be circulated only if sufficient funds have been deposited with the Trustee to pay the prepayment price of the 1996 Certificates to be prepaid.

Notice of such prepayment shall be mailed first class postage prepaid to the Remarketing Agent and Securities Depositories and the respective Owners designated for prepayment at their addresses appearing on the Certificate registration books at least thirty (30) days but not more than sixty (60) days (five days with respect to optional prepayment of 1996 Certificates prior to the prepayment date), which notice shall, in addition to setting forth the above information, set forth, in the case of each Certificate called only in part, the portion of the principal thereof which is to be prepaid.

Neither failure to receive such notice nor any immaterial defect in any notice so mailed shall affect the sufficiency of the proceedings for the prepayment of such 1996 Certificates.

***Partial Prepayment of Certificate.*** Upon surrender of any Certificate prepaid in part only, the Trustee shall execute and deliver to the Owners, at the expense of the District, a new Certificate or 1996 Certificates of authorized denominations equal in aggregate principal amount to the unprepaid portion of the Certificate surrendered and of the same interest rate and the same maturity. Such partial prepayment shall be valid upon payment of the amount thereby required to be paid to such Owner, and the District, the Corporation and the Trustee shall be released and discharged from all liability to the extent of such payment.

*Effect of Notice of Prepayment.* Notice having been given as aforesaid, and the moneys for the prepayment (including the interest to the applicable date of prepayment), having been set aside in the Certificate Payment Fund, the 1996 Certificates called for prepayment shall become due and payable on said date of prepayment, and, upon presentation and surrender thereof at the office or offices specified in said notice, said 1996 Certificates shall be paid at the unpaid principal amount with respect thereto, plus premium, if any, and interest accrued and unpaid to said date of prepayment.

If, on said date of prepayment, moneys for the prepayment of all the 1996 Certificates to be prepaid, together with interest to said date of prepayment, shall be held by the Trustee so as to be available therefor on said date of prepayment, and if notice of prepayment thereof shall have been given as aforesaid, then, from and after said date of prepayment, interest with respect to the 1996 Certificates called for prepayment shall cease to accrue and become payable. All moneys held by or on behalf of the Trustee for the prepayment of 1996 Certificates shall be held in trust for the account of the Owners so to be prepaid.

## **SPECIAL CONSIDERATIONS RELATING TO THE 1996 CERTIFICATES SUBJECT TO OPTIONAL TENDER AND REMARKETING**

### **The Remarketing Agent is Paid by the District**

The Remarketing Agent's responsibilities include determining the interest rate from time to time and remarketing 1996 Certificates that are optionally or mandatorily tendered by the owners thereof (subject, in each case, to the terms of the Remarketing Agreement), as further described in this Reoffering Memorandum. The Remarketing Agent is appointed by the District and is paid by the District for its services. As a result, the interests of the Remarketing Agent may differ from those of existing holders and potential purchasers of 1996 Certificates.

### **The Remarketing Agent Routinely Purchases 1996 Certificates for Its Own Account**

The Remarketing Agent acts as remarketing agent for a variety of variable rate demand obligations and, in its sole discretion, routinely purchases such obligations for its own account. The Remarketing Agent is permitted, but not obligated, to purchase tendered 1996 Certificates for its own account and, in its sole discretion, routinely acquires such tendered 1996 Certificates in order to achieve a successful remarketing of the 1996 Certificates (i.e., because there otherwise are not enough buyers to purchase the 1996 Certificates) or for other reasons. However, the Remarketing Agent is not obligated to purchase 1996 Certificates, and may cease doing so at any time without notice. The Remarketing Agent may also make a market in the 1996 Certificates by routinely purchasing and selling 1996 Certificates other than in connection with an optional or mandatory tender and remarketing. Such purchases and sales may be at or below par. However, the Remarketing Agent is not required to make a market in the 1996 Certificates. The Remarketing Agent may also sell any 1996 Certificates it has purchased to one or more affiliated investment vehicles for collective ownership or enter into derivative arrangements with affiliates or others in order to reduce its exposure to the 1996 Certificates. The purchase of 1996 Certificates by the Remarketing Agent may create the appearance that there is greater third party demand for the 1996 Certificates in the market than is actually the case. The practices described above also may result in fewer 1996 Certificates being tendered in a remarketing.

## **1996 Certificates May Be Offered at Different Prices on Any Date Including a Rate Determination Date**

Pursuant to the Remarketing Agreement, the Remarketing Agent is required to determine the applicable rate of interest that, in its judgment, is the lowest rate that would permit the sale of the 1996 Certificates bearing interest at the applicable interest rate at par plus accrued interest, if any, on and as of the commencement of the applicable Weekly Rate Period. The interest rate will reflect, among other factors, the level of market demand for the 1996 Certificates (including whether the Remarketing Agent is willing to purchase 1996 Certificates for its own account). There may or may not be 1996 Certificates tendered and remarketed on the commencement of the applicable Weekly Rate Period, the Remarketing Agent may or may not be able to remarket any 1996 Certificates tendered for purchase on such date at par and the Remarketing Agent may sell 1996 Certificates at varying prices to different investors on such date or any other date, The Remarketing Agent is not obligated to advise purchasers in a remarketing if it does not have third party buyers for all of the 1996 Certificates at the remarketing price. In the event that the Remarketing Agent owns any 1996 Certificates for its own account, it may, in its sole discretion in a secondary market transaction outside the tender process, offer such 1996 Certificates on any date, including the date of the commencement of the applicable Weekly Rate Period, at a discount to par to some investors.

## **The Ability to Sell the 1996 Certificates Other Than through Tender Process May Be Limited**

The Remarketing Agent may buy and sell 1996 Certificates other than through the tender process. However, it is not obligated to do so and may cease doing so at any time without notice and may require holders that wish to tender their 1996 Certificates to do so through the Tender Agent with appropriate notice. Thus, investors who purchase the 1996 Certificates, whether in a remarketing or otherwise, should not assume that they will be able to sell their 1996 Certificates other than by tendering the 1996 Certificates in accordance with the tender process.

## **SOURCES AND USES OF FUNDS**

The sources and uses of funds with respect to initial delivery of the 1996 Certificates were as follows:

### ***Sources***

Principal Amount of 1996 Certificates	<u>\$15,400,000</u>
Total	<u>\$15,400,000</u>

### ***Uses***

Deposit to Acquisition Fund	\$15,192,645
Underwriter's Discount	22,355
Costs of Issuance <sup>(1)</sup>	<u>185,000</u>
Total	<u>\$15,400,000</u>

<sup>(1)</sup> Included legal, financing and consulting fees, fees associated with the letter of credit, rating agency fees, printing costs and other miscellaneous expenses.

## **Letter of Credit**

On June 30, 2011, the Letter of Credit is expected to be replaced the existing irrevocable, direct-pay letter of credit dated issued by Landesbank Hessen-Thüringen Girozentrale (Helaba). The Letter of Credit is issued for the benefit of the 1996 Certificates to provide the payment of principal and Purchase Price of, and interest with respect to, the 1996 Certificates as described under the caption “THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT.” Prior to the expiration date of the Letter of Credit, the 1996 Certificates will be subject to mandatory purchase. See the caption “THE CERTIFICATES - Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit.”

## **Alternate Letter of Credit**

The Trust Agreement provides that if at any time there has been delivered to the Trustee: (i) a Substitute Facility in substitution for the Letter of Credit then in effect; (ii) an opinion of counsel stating that the delivery of such Substitute Facility to the Trustee is authorized under the Trust Agreement and complies with the terms thereof; (iii) ) an Opinion of Bond Counsel that the proposed substitution will not adversely affect the exclusion of interest on the 1996 Certificates from gross income for federal income tax purposes; (iv) one or more opinions of counsel addressed to the Trustee, to the effect, singly or together, that: (A) the Substitute Facility is a legal, valid and binding obligation of the obligor, enforceable against the obligor in accordance with its terms, except as limited by applicable reorganization, insolvency, liquidation, readjustment of debt, moratorium or other similar laws affecting the enforcement of the rights of creditors generally as such laws may be applied in the event of a reorganization, insolvency, liquidation, readjustment of debt or other similar proceeding of or moratorium applicable to the obligor and by general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law); and (B) payments made by the obligor under the Substitute Facility will not be voidable under Section 547 of the United States Bankruptcy Code in the context of a case or proceeding by or against the District or any Affiliates thereof under the United States Bankruptcy Code; (v) if a rating or ratings on the Certificates shall be in effect on the date of such substitution, written evidence from Moody’s and/or Standard & Poor’s, as applicable, to the effect that such rating agency has reviewed the proposed Substitute Facility and that the substitution of the proposed Substitute Facility for the existing Facility will not, by itself, result in a reduction or withdrawal of its rating on the Certificates; and (vi) written evidence that notice of such proposed substitution has been sent to the Owners prior to such substitution, then the Trustee shall, so long as such Substitute Facility shall contain administrative procedures which are acceptable to the Trustee in its reasonable discretion, accept such Substitute Facility and promptly surrender the existing Facility to the issuer thereof, and surrender the Letter of Credit then in effect to the Bank. The 1996 Certificates will be subject to mandatory tender for purchase on the substitution date. See the caption “THE CERTIFICATES - Mandatory Tenders Upon Expiration, Substitution or Termination of Letter of Credit.”

## **THE LETTER OF CREDIT AND THE REIMBURSEMENT AGREEMENT**

*The following information has been provided by the Bank for use in this Reoffering Memorandum. Such information has not been confirmed or verified by the District or the Remarketing Agent. Neither the District nor the Remarketing Agent make any representation as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof. Further, no representation is made herein that the information contained or incorporated herein by reference is correct as of any time subsequent to the date hereof.*

The Irrevocable Letter of Credit (the “Letter of Credit”) will be issued by the Bank pursuant to the Reimbursement Agreement dated as of June 30, 2011 (the “Reimbursement Agreement”), by and between the District and the Bank. The following summarizes certain provisions of the Letter of Credit and the Reimbursement Agreement, to which documents reference is made for the complete provisions thereof.

The provisions of any substitute letter of credit and related reimbursement agreement may be different from those summarized below.

## **Letter of Credit**

(to be conformed when draft LOC is received)

The 1996 Certificates are secured by the Letter of Credit issued by the Bank pursuant to the Reimbursement Agreement. The Letter of Credit will expire on the date that is the earliest of (a) June 30, 2014, provided however, the District may request the Bank to extend the Letter of Credit by making such a request not less than six months prior to the expiration date, but extension of the expiration date of the Letter of Credit is solely at the Bank's discretion; (b) the date on which the Bank honors a payment on the Letter of Credit in connection with the purchase or redemption of all of the Bonds, the conversion of the interest rate on the Bonds or a final payment with respect to the Bonds; (c) fifteen (15) days after receipt by the Trustee of written notice from the Bank directing the Trustee to purchase or redeem all outstanding Bonds and present a final drawing under the Letter of Credit as a result of the occurrence of an Event of Default under the Reimbursement Agreement; or (d) the date on which the Letter of Credit is surrendered by the Trustee to the Bank.

While in effect, the Letter of Credit entitles the Trustee to draw on the Letter of Credit, on such dates and at such times as are specified in the Letter of Credit. Each drawing honored by the Bank under the Letter of Credit will immediately reduce the Stated Amount by the amount of such drawing, subject to reinstatement on the terms set forth in the Letter of Credit. All drawings under the Letter of Credit will be paid with the Bank's own funds.

## **Reimbursement Agreement**

(to be conformed when draft Reimbursement Agreement is received)

The Bonds are initially supported by the Initial Letter of Credit which will be issued by the Bank pursuant to the provisions of the Reimbursement Agreement. The Bank has entered into the Reimbursement Agreement with the District providing for, among other things, the District's reimbursement to the Bank of all amounts drawn upon under the Letter of Credit.

The Reimbursement Agreement provides for commitment fees, drawing fees, transfer fees and other fees and charges. The District's obligations under the Reimbursement Agreement are to be secured by the Net Revenues and Taxes.

The District has made comprehensive representations and warranties about itself and its operations in the Reimbursement Agreement to induce the Bank to issue the Initial Letter of Credit. These representations and warranties include, among others, \_\_\_\_\_. The Reimbursement Agreement contains affirmative and negative covenants and reporting requirements. The covenants of the District include, among others: \_\_\_\_\_. Reporting requirements include requirements to furnish \_\_\_\_\_.

The Reimbursement Agreement also sets out certain Events of Default. These include, among others: (i) failure to pay any amount due the Bank; (ii) any attachment of Trust Agreement or Installment Agreement funds; (iii) failure of any representation or warranty to have been true in any material respect; (iv) loss of tax exemption; (v) any default under documents entered into with the Bank or if any event of default occurs under the Trust Agreement or Installment Agreement; (vi) dissolution or insolvency of the District or bankruptcy, reorganization or similar proceedings affecting the District, other than involuntary proceedings dismissed within 60 days; (vii) any execution or similar process in excess of \$500,000 remaining outstanding against the District for 10 days; (viii) failure to maintain required permits or licenses; (ix) failure to comply with governmental regulatory agreements affecting the Project; (x) failure

to maintain insurance on the Project, to protect against liens, or failure to perform covenants in the Reimbursement Agreement within certain cure periods; (xi) default under any other indebtedness of the District; and (xii) failure to comply with its financial covenants.

Upon the occurrence of an Event of Default under the Reimbursement Agreement, the Bank may: (i) call all or a portion of the 1996 Certificates for redemption in accordance with the Trust Agreement; (ii) declare a mandatory tender of the 1996 Certificates in accordance with the Trust Agreement; (iii) request that all 1996 Certificates be tendered for purchase as 1996 Certificates to be owned by the Bank; (iv) enforce its rights against the District through legal action; and (v) exercise other remedies under applicable law or other agreements.

The Bank and the District may, from time to time, amend the Reimbursement Agreement without notice to, or consent of, the Trustee or the Owners.

## **THE BANK**

*The following information has been provided by the Bank for use in this Reoffering Memorandum. Such information has not been confirmed or verified by the District or the Remarketing Agent. Neither the District nor the Remarketing Agent make any representation as to the accuracy or adequacy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof. Further, no representation is made herein that the information contained or incorporated herein by reference is correct as of any time subsequent to the date hereof.*

### **Union Bank, N.A.**

Union Bank is a full-service commercial bank providing an array of financial services to individuals, small businesses, middle-market companies, and major corporations. The Bank operates 401 branches and 617 ATM's in California, Oregon, Washington, and Texas, as well as two international offices. The Bank serves corporate clients across the country, and has a retail customer base of approximately 1 million households.

Union Bank, N.A. is the primary subsidiary of UnionBanCal Corporation, the second-largest commercial bank holding company headquartered in California, based on assets of \$80.6 billion at March 31, 2011. UnionBanCal is a wholly owned subsidiary of The Bank of Tokyo-Mitsubishi UFJ, Ltd., and a member of the Mitsubishi UFJ Financial Group (MUFG, NYSE:MTU), one of the world's largest financial organizations.

For the quarter ending March 31, 2011, the Corporation had loans totaling \$48.1 billion, total assets of \$80.6 billion and total deposits of \$58.7 billion. For fiscal year ended December 31, 2010, a net income of \$573.0 million was reported, compared with a net loss of \$65 million for full year 2009. Copies of the latest annual report and the most recent quarterly report may be obtained at [www.unionbank.com](http://www.unionbank.com) or at the Bank's Los Angeles office, located at 445 South Figueroa Street, Los Angeles, California 90071.

# SOURCES OF PAYMENT FOR THE CERTIFICATES

## General

Each 1996 Certificate represents a direct, undivided fractional interest in the Installment Payments to be made by the District to the Corporation under the Installment Sale Agreement. The Corporation has assigned all of its rights under the Installment Sale Agreement, including its rights to receive Installment Payments from the District and its remedies under the Installment Sale Agreement to the Trustee for the benefit of the Owners of the 1996 Certificates. The Installment Payments are sufficient to pay, when due, the annual principal and interest represented by the 1996 Certificates.

## Installment Payments

Pursuant to the Installment Sale Agreement, the District is obligated to make Installment Payments solely from Taxes and Net Revenues. The combined totals of such Installment Payments equals the principal and interest due with respect to the 1996 Certificates. The obligation of the District to make the Installment Payments is absolute and unconditional, and until such time as the Purchase Price shall have been paid in full (or provision for the payment thereof shall have been made pursuant to the Installment Purchase Agreement), the District will not discontinue or suspend any Installment Payment required to be made by it under the Installment Sale Agreement when due, whether or not the Water System or any part thereof is operating or operable or its use is suspended, interfered with, reduced or curtailed or terminated in whole or in part, and such payments shall not be subject to reduction whether by offset or otherwise and shall not be conditional upon the performance or nonperformance by any party of any agreement for any cause whatsoever.

**The District's obligation to make the Installment Payments is a limited obligation of the District payable solely from Taxes and Net Revenues of the Water System, and neither the full faith and credit nor the taxing power of the District, the State of California or any of its political subdivisions is pledged for the payment of the 1996 Certificates.**

## Taxes and Net Revenues

The Installment Payments securing the 1996 Certificates are payable from Taxes and Net Revenues on a parity with installment payments securing the District's 2004 Certificates and the 2007 Certificates and the Otay Water District Financing Authority's 2010 Bonds.

"Taxes" means all taxes, including *ad valorem* taxes of the District, other than taxes imposed pursuant to Chapter 1 of Part 9 of the Law to secure general obligation bonds of the District or any improvement district thereof.

"Revenues" means (i) all water availability charges imposed pursuant to Chapter 2 of Part 5 of the Law not exceeding \$10 per acre per year; (ii) all income, rents, rates, fees, charges and other moneys derived by the District from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (a) all income, rents, rates, fees, charges or other moneys derived from the sale, furnishing, and supplying of water and other services, facilities and commodities sold, furnished or supplied through the facilities of the Water System, including connection fees, (b) the earnings on and income derived from the investment of such income, rents, rates, fees and charges or other moneys, (c) the proceeds derived by the District directly or indirectly from the sale, lease or other disposition of a part of the Water System as permitted under the Installment Purchase Agreement and (d) Interest Subsidy Payments; provided that the term "Revenues" shall not include customers' deposits or any other deposits subject to refund until such deposits have become the property of the District.

“Operation and Maintenance Costs” means (i) costs spent or incurred for maintenance and operation of the Water System calculated in accordance with generally accepted accounting principles, including (among other things) the reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the District that are charged directly or apportioned to the Water System, including but not limited to salaries and wages of employees, payments to the Public Employees Retirement System, overhead, insurance, taxes (if any), fees of auditors, accountants, attorneys or engineers and insurance premiums, and including all other reasonable and necessary costs of the District or charges (other than debt service payments) required to be paid by it to comply with the terms of the Bonds or of the Installment Purchase Agreement or any Contract or of any resolution or indenture authorizing the issuance of any Bonds or of such Bonds; and (ii) costs spent or incurred in the purchase of water for the Water System; but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature and all capital charges.

“Net Revenues” means, for any Fiscal Year or other 12-month period, the Revenues for such Fiscal Year or other 12-month period less the Operation and Maintenance Costs for such Fiscal Year or other 12-month period. See “Rate Covenant” and “Parity Debt” herein.

“Interest Subsidy Payment” means cash subsidy payments entitled to be received by the District from the United States Treasury with respect to the 2010B Bonds and any Parity Bonds issued and Contracts executed by the District, including but not limited to “Build America Bonds” issued as contemplated by the American Recovery and Reinvestment Act of 2009.

The District will timely submit all required documentation to the United States Treasury and take any and all action necessary to receive and collect the Interest Subsidy Payments.

## **Allocation of Taxes and Revenues**

Pursuant to the Installment Sale Agreement, the 2004 Installment Purchase Agreement, the 2007 Installment Purchase Agreement and the 2010 Installment Purchase Agreement (collectively, the “Agreements”), the District established separate special funds, the “Revenue Fund” and the “Tax Fund.” Under the Agreements, the District has agreed to deposit all Revenues in the Revenue Fund and all Taxes in the Tax Fund. The Revenues and Taxes will not be used for any other purpose while any of the installment payments due under the Agreements remain unpaid, except as described below. Under the terms of the Agreements, the District will, from moneys in the Revenue Fund, pay Operation and Maintenance Costs (including amounts reasonably required to be set aside in contingency reserves for Operation and Maintenance Costs, the payment of which is not then immediately required) as they become due and payable.

All moneys in the Tax Fund, and, to the extent such moneys are insufficient, all remaining moneys in the Revenue Fund, shall be set aside by the District at the following times in the following respective special funds in the following order of priority and all moneys in each of such funds shall be held in trust and shall be applied, used and withdrawn only for the purposes described herein:

- (a) *Certificate Payment Fund.* On or before each Installment Payment Date, the District shall, from the moneys in the Tax Fund and, to the extent needed, the Revenue Fund, transfer to the Trustee for deposit in the Certificate Payment Fund, the Installment Payment due and payable on that Installment Payment Date. The District shall also, from the moneys in the Tax Fund and, to the extent needed, the Revenue Fund, transfer to the applicable trustee or payee for deposit in the applicable payment fund, without preference or priority, and in the event of any insufficiency of such moneys ratably without any discrimination or preference, payments due under the Agreements and payments with respect to any additional Contracts.

No deposit need be made in the Certificates Payment Fund as Installment Payments if the amount in the Certificates Payment Fund is at least equal to the amount of the Installment Payment due and payable on the next succeeding Installment Payment Date.

All money in the Certificates Payment Fund shall be used and withdrawn by the Trustee in accordance with the Trust Agreement.

- (b) *Reserve Fund.* On or before each Installment Payment Date, the District shall, from the remaining moneys in the Tax Fund and, to the extent needed, the Revenue Fund, thereafter, without preference or priority, and in the event of any insufficiency of such moneys ratably without any discrimination or preference, transfer to the applicable trustee for deposit to such other reserve fund or account for the Existing Parity Obligations and payments with respect to any additional Contracts an amount equal to the amount required to be deposited therein, and to transfer to any insurer any amounts due pursuant to any agreement related to the repayment of draws under a Reserve Policy.

No transfer of moneys for deposit to the Reserve Fund in connection with the Installment Payments need be made if the amount contained therein is at least equal to the Reserve Fund Requirement.

- (c) *Surplus.* Moneys on deposit in the Tax Fund or Revenue Fund not necessary to make any of the payments required above or as required under the Agreements or with respect to any additional Contracts may be expended by the District at any time for any purpose permitted by law.

## **Event of Default and Acceleration of Maturities**

The Installment Payments are payable only from Taxes and Net Revenues and are not secured by, and the 1996 Certificate Owners have no security interest in or mortgage on the property of the Water System or any other assets of the District. Should the District default, the Trustee, as assignee of the Corporation, shall have the right at its option and without any further demand or notice, but subject in all respects to the provisions of the Trust Agreement, declare the entire principal amount of the unpaid Installment Payments and the accrued interest thereon to be due and payable immediately, and upon any such declaration the same shall become immediately due and payable, anything contained in the Installment Sale Agreement to the contrary notwithstanding. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE TRUST AGREEMENT - Default and Limitation of Liability" and "SUMMARY OF CERTAIN PROVISIONS OF THE INSTALLMENT PURCHASE AGREEMENT - Events of Default and Remedies."

## **Rate Covenant**

Pursuant to the Agreements, the District will fix, prescribe, revise and collect rates, fees and charges for the Water Service which will be at least sufficient to yield during each Fiscal Year Taxes and Net Revenues equal to 125% of the Debt Service (including for purposes of such calculation the obligation of the District to repay costs related to any surety bond, reserve credit facility or other reserve fund funding instrument) on the 1996 Certificates, the Existing Parity Obligations and additional Contracts or Parity Bonds (as defined herein) for such Fiscal Year. The District may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Taxes and Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of the Agreements.

For purposes of calculating the ratio required by the rate covenant, when the Existing Parity Obligations are no longer outstanding, the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

For the purposes of the calculations described above, the adjustments to Net Revenues and Debt Service relating to the Interest Subsidy Payments will be made when the Existing Parity Obligations are no longer outstanding with respect to the 2010B Bonds or with respect to any Parity Bonds or additional Contracts that are designated as “Build America Bonds.” See “APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

## **Parity Debt**

Pursuant to the Agreements, the District may at any time execute any contract or issue any bonds the payments under or of which are on a parity with the Installment Payments (“Contracts” or “Parity Bonds”), as the case may be, provided an Independent Financial Consultant or Certified Public Accountant shall render to and file with the District and the Trustee a written report certifying that Taxes and Net Revenues for any twelve (12) consecutive calendar months in the eighteen (18) calendar months immediately preceding the issuance of the additional Contracts or Parity Bonds adjusted as set forth below are at least equal to 125% of Debt Service (including for purposes of such calculation the obligation of the District to repay costs related to any surety bond, reserve credit facility or other reserve fund funding instrument), assuming such additional Contracts had been executed or Parity Bonds had been issued at the beginning of such twelve-month period.

For purposes of calculating the ratio required for the issuance of additional Contracts or Parity Bonds, when the Existing Parity Obligations are no longer outstanding (with the exception of the 2010 Bonds), the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

For the purposes of the calculations described above, the adjustments to Net Revenues and Debt Service relating to the Interest Subsidy Payments will be made when the Existing Parity Obligations are no longer outstanding with respect to the 2010B Bonds or with respect to any Parity Bonds or additional Contracts that are designated as “Build America Bonds.”

For purposes of calculating Net Revenues as set forth in the preceding paragraph, adjustments to the computations of Net Revenues may be made for the following:

- (1) any change in service charges which has been adopted subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts;
- (2) customers added to the Water System subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts;
- (3) the estimated change in Net Revenues which will result from the connection of existing residences or businesses to the Water System within one year following completion of any project to be funded or system to be acquired from the proceeds of such Parity Bonds or additional Contracts; and

- (4) the estimated change in Net Revenues which will result from services provided under any long-term, guaranteed contract that extends for the life of the Parity Bonds or additional Contracts if entered into subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the Parity Bonds or additional Contracts.

Notwithstanding the foregoing, Parity Bonds issued or additional Contracts executed to refund Parity Bonds or additional Contracts (including refunding of the Existing Parity Obligations or the Bonds), may be delivered without satisfying the conditions set forth above if Debt Service in each Fiscal Year after the Fiscal Year in which such Parity Bonds are issued or additional Contracts executed is not greater than Debt Service would have been in each such Fiscal Year prior to the issuance of such Parity Bonds or execution of such additional Contracts. Further, for the purpose of calculating Debt Service for any Parity Bonds or additional Contracts which bear a variable interest rate, the rate of interest used to calculate Debt Service shall be 110% of the greater of (i) the then current variable interest rate borne by such Parity Bonds or additional Contracts (which includes outstanding 1996 Certificates) plus 2%, and (ii) the highest variable rate borne over the preceding 12 months by outstanding variable rate debt issued by the District or, if no such variable rate debt is at the time outstanding, by variable rate debt of which the interest rate is computed by reference to an index comparable to that to be utilized in determining the interest rate for the debt then proposed to be issued. See "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

In addition to the foregoing, in the event any amounts that are past due and owing to any insurer of Bonds or with respect to any Contracts, such insurer must provide written consent to the issuance of any additional Bonds or the execution of any Contracts.

## **Property Insurance**

The Installment Sale Agreement requires the District to maintain or cause to be maintained with respect to the properties of the Water System, insurance in such amounts and against such risks (including accident to or destruction of the Water System which are of an insurable nature) as are usually covered in connection with facilities similar to the Water System so long as such insurance is available at reasonable costs (see "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE INSTALLMENT SALE AGREEMENT - Insurance" herein). Any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and in the manner usually maintained in connection with water systems similar to the Water System. All proceeds of insurance against property damage and all proceeds of condemnation awards relating to the Project shall be payable to the District alone, and the District shall retain and collect such proceeds. All claims under any such insurance policy or with respect to any condemnation proceeding relating to the Project may be settled by the District without the consent of the Corporation or the Trustee. Such proceeds shall be applied promptly to the optional prepayment of Installment Payments, or retained by the District and promptly applied to the repair or rebuilding of the Project or the acquisition or construction of the capital improvements to the Water System. See "THE CERTIFICATES - Prepayment - Prepayment From Net Proceeds of Insurance and Condemnation" herein. See also "APPENDIX A - SUMMARY OF PRINCIPAL LEGAL DOCUMENTS - THE INSTALLMENT SALE AGREEMENT - Insurance" herein.

## OTAY WATER DISTRICT

The District was formed in January 1956 pursuant to Section 71000 et seq., of the California Water Code, and joined the San Diego County Water Authority (which is a member of the Metropolitan Water District of Southern California) in September 1956 to acquire the right to purchase and distribute imported water throughout its service area. The District's boundaries currently encompass an area of approximately 125 square miles in San Diego County, lying immediately east of the San Diego metropolitan area and running from the City of El Cajon south to the Mexican border, abutting the cities of El Cajon and La Mesa, and encompassing most of the City of Chula Vista and a small portion of the City of San Diego (the "Service Area"). The District is the sole provider of water in the Service Area. Approximately 39% of the geographic Service Area is currently developed, and this percentage will continue to increase as the District's Service Area continues to develop and grow. The District's water sales by volume increased by 7.5% per year from 2004 to 2007. Since 2007, new residential construction has declined significantly and there has been little growth in residential connections. However, the District continues to add connections to both its potable and recycled water system at a slow rate. As of June 30, 2010, the District had nearly 48,000 potable and 700 recycled service accounts representing a population of approximately 206,000, with an average daily demand of 30.5 million gallons per day (mgd). Ultimately, the District is projected to serve 277,000 people, creating an average daily demand of 56.3 mgd.

Most potable water delivered by the District is purchased from the San Diego County Water Authority ("SDCWA") who in turn purchases water from the region's water importer, the Metropolitan Water District of Southern California and QSA supplies. In Fiscal Year 2007, the District entered into an agreement with the City of San Diego to treat raw water to potable level before being introduced to the District's Water System. A small amount of potable water has also been purchased from the City of San Diego, and will be purchased in the future on an as needed basis. By taking raw water through SDCWA's system at a different connection, there is increased reliability of water supplied to the District. In addition, the Jamacha Road Pipeline Project provides increased capacity with the connection to SDCWA, where the District has established an additional delivery point for treated water from the Helix Water District Levy treatment plant. Water delivered through the new pipeline will be stored in two recently constructed 10 million gallon reservoirs. The District is also moving forward with a ground water project which will provide an additional source of water.

The District owns and operates a recycled water distribution network. Recycled water from the District's Ralph W. Chapman Water Recycling Facility ("RWCWRF") is used to irrigate golf courses, landscaping at schools, public parks, roadway landscapes, and various other approved uses in eastern Chula Vista. The RWCWRF is capable of reclaiming wastewater at a rate of approximately 1.2 million gallons per day. The District is also in a partnership with the City of San Diego to beneficially reuse an additional 6 million gallons per day of recycled water from the City of San Diego's South Bay Reclamation Plant (since Spring of 2007), which required the District to construct over six miles of connecting pipeline, a pump station and a 12 million gallon reservoir. Using this new resource to meet recycled water demands on the Water System has resulted in the District being able to allocate approximately 3,100 acre-feet per year of potable water to other uses.

The District also owns and operates a wastewater collection and reclamation system, providing public sewer service to approximately 4,656 customers within the Jamacha drainage basin. This wastewater system is not a part of the Water System.

The District is administered by a Board of Directors consisting of five members who are elected to four-year alternating terms by the voters residing within the District's boundaries. The District is divided into five divisions, with each Director representing a specific division within which he or she must reside. The current members of the Board and key administrative personnel are:

### **DIRECTORS**

Jaime Bonilla, *President - Division 2*  
Gary D. Croucher, *Vice President - Division 3*  
David Gonzalez, Jr., *Treasurer - Division 1*  
Jose Lopez, *Division 4*  
Mark Robak, *Division 5*

### **MANAGEMENT TEAM**

Mark Watton, *General Manager*  
German Alvarez, *Assistant General Manager Finance & Administration*  
Manny Magaña, *Assistant General Manager Engineering & Operations*  
Joseph R. Beachem, *Chief Financial Officer*  
Rom Sarno, Jr., *Chief of Administrative Services*  
Geoff Stevens, *Chief Information Officer*  
Rod Posada, *Chief of Engineering*  
Pedro Porras, *Chief of Water Operations*

Under direction of the General Manager, the District has 159 employees.

## **THE WATER SYSTEM**

The following information concerning the Water System was obtained from District officials except where otherwise indicated. The audited financial statements of the District for the Fiscal Year ended June 30, 2010 are attached hereto as "APPENDIX B" and should be read in their entirety.

### **Existing Facilities**

Potable Water Facilities - The principal facilities of the existing potable water system consist of six water supply connections with SDCWA, one water supply connection with the City of San Diego, 24 pump stations, over 709 miles of pipelines, and 40 storage reservoirs.

The District currently receives treated potable water from the SDCWA through four connections to one of the pipelines owned and operated by the SDCWA. This water is treated by the Metropolitan Water District of Southern California at its Skinner Water Treatment Plant and SDCWA at its Twin Oaks Treatment Plant. In addition, the District currently receives treated potable water from the SDCWA through one connection to the Helix Water District water system. This water is be treated by the Helix Water District at its R.M. Levy Water Treatment Plant pursuant to an agreement with the SDCWA. The District may also purchase treated potable water, if available, from the City of San Diego. This water is sold by the SDCWA to the District in raw form and delivered to the City of San Diego's Otay Water Treatment Plant pursuant to an agreement among the SDCWA, the District and the City of San Diego. These supply sources and connecting transmission mains deliver water to terminal storage reservoirs that provide water service to customers within the Service Area.

Recycled Water Facilities - The principal facilities of the existing recycled water system consist of 2 recycled water supply sources, 3 pump stations, 96 miles of pipelines, and 4 storage reservoirs.

The District currently produces recycled water at the RWCWRF, which is owned and operated by the District. Recycled water from the RWCWRF and some of the District’s treated potable water supply are delivered into storage reservoirs that provide recycled water service to recycled water customers.

The District is divided into five geographic areas. These five areas contain five potable water systems and two recycled water systems. The systems are called Hillsdale, Regulatory, La Presa, Central Area, and Otay Mesa. The Hillsdale, Regulatory, and La Presa systems are collectively referred to as the North District, while the Central Area and Otay Mesa systems are collectively referred to as the South District. Recycled water service is currently limited to the South District. There are multiple pressure zones within each system, except Otay Mesa.

**North District.** The Hillsdale system includes the extreme north part of the District’s Service Area. The Regulatory system is located between the Hillsdale and La Presa systems. The Regulatory system reservoirs are considered to provide emergency storage for the entire North District as well as some operational storage for the 640 and 520 Pressure Zones. Two new 10 million gallon reservoirs are located within the Regulatory system and provide storage for the treated water delivered through the new 36 inch pipeline, which connects to the Helix Water District system by way of the SDCWA aqueduct. The La Presa system is generally located north and east of the Sweetwater reservoir and is the southernmost system of the North District.

**South District.** The Central Area system is roughly bounded by Interstate 805 on the west, Otay River on the south, the Lower Otay Reservoir on the east, and the Regulatory System on the north. Three Central Area system reservoirs provide emergency storage for the entire Central Area system and also provide operational storage for the 624 Pressure Zone. Additional reservoirs provide operational storage for other pressure zones throughout the Central Area. The Otay Mesa system includes the extreme south portion of the District Service Area and is generally located between the Otay River on the north and the Mexico border on the south. The South District has experienced, and is expected to experience, the most growth in the District’s Service Area.

## Water Storage

The District currently operates 41 potable and 4 recycled reservoirs as shown below with a total capacity of 263 mg. The District estimates that the reservoirs are between 75% and 80% full on a typical day.

<u>System</u>	<u>Reservoirs</u>	<u>Capacity (mg)</u>
Hillsdale	6	13.9
Regulatory	13	48.7
La Presa	9	23.7
Central Area	11	85.5
Otay Mesa	2	47.7
Recycled	<u>4</u>	<u>43.7</u>
Total	45	263.2

## Water Supply

**Service Area Water Supply - Potable.** The District does not have a local source of surface water, and is working to complete a modest supply of ground water. The District purchases a significant amount of its potable water from the SDCWA. Under a contractual arrangement with the SDCWA, the District also receives potable water from the Helix Water District's Levy Water Treatment Plant and from the City of San Diego.

The SDCWA implemented a water rate increase on January 1, 2010, which resulted in an approximate 11.3% increase for the District's cost of purchased potable water from SDCWA. SDCWA has provided preliminary estimates on water cost increase expected to be implemented by SDCWA January 1, 2011. The overall cost increase is expected to be 7.5%.

**Service Area Water Supply - Recycled.** The District produces approximately 1.2 mgd of recycled water at the RWCWRF. The District has contracted with the City of San Diego to purchase up to 6 mgd of recycled water produced by the City of San Diego's South Bay Water Reclamation Plant. Construction on the required pump station, reservoir, and the 6-mile delivery system allowing the District to connect to the City of San Diego's recycled water pipeline was completed in 2007.

**SDCWA Water Supply.** For Fiscal Year 2010, approximately 87% of the region's water supply came from imported water, with the remainder coming from member agency's local supplies. Of the purchased supply, 71% is from the Metropolitan Water District of Southern California ("MWD"). For the Fiscal Year ended June 30, 2010, the SDCWA supplied the District 31,168 acre-feet of water (quantities of water are expressed in terms of acre-feet which is the amount of water which will cover one acre to a depth of one foot and is equivalent to approximately 326,000 gallons and approximately the average annual water usage of two households).

As an alternative to purchasing all of its imported water from MWD, the SDCWA has begun to diversify its purchases through core and spot water transfers with other agencies. Since 2003, the SDCWA has been receiving a portion of its imported water pursuant to the terms of the Quantification Settlement Agreement ("QSA") among the State of California acting by and through the Department of Fish and Game, the Coachella Valley Water District ("CVWD"), the Imperial Irrigation District ("IID") and the SDCWA, executed on October 10, 2003, the Water Transfer Agreement (defined below) and other QSA related agreements. Water that the SDCWA receives from IID is conveyed through the Colorado River Aqueduct pursuant to an exchange agreement with MWD. The SDCWA began receiving transfer water from IID in December 2003. Starting with the initial delivery of 10,000 acre-feet, the amount of water to be delivered is increasing according to an agreed-upon schedule until the maximum transfer yield of 200,000 acre-feet per year is achieved. In addition, the SDCWA will receive approximately 77,000 acre-feet of imported water per year from water conserved through the lining of the All-American Canal Lining Project and the Coachella Canal Lining Project. The SDCWA began receiving water from the Coachella Canal Lining Project in 2007 and in 2010 will receive its full allotment from the All-American Canal Lining Project. The SDCWA is also pursuing spot water transfers to provide supplemental supplies to the region during times of supply shortages. Spot transfers are short-term transfers or leases, typically agreed to and completed within one to three years.

Litigation related to the QSA is described in "APPENDIX F - INFORMATION CONCERNING METROPOLITAN WATER DISTRICT'S WATER SUPPLY - QSA-Related Litigation."

The SDCWA continues to pursue supply diversification efforts for itself and the region, including long-term planning, recycling of local surface water, groundwater, recycled water, local seawater desalination and conservation efforts.

Water Storage facilities are also critical to assuring consistent water availability notwithstanding fluctuation in available supply. The SDCWA has recently entered into agreements to expand available storage capacity. The SDCWA recently issued over \$600 million in water bonds to finance its Capital Improvement Program. One of the purposes of the Capital Improvement Program is to interconnect a number of member agency storage facilities. Another purpose is to enhance the SDCWA's own storage capacity.

The SDCWA faces various challenges in the continued supply of water to the District and other member agencies. A description of these challenges as well as a variety of other operating information with respect to the SDCWA is included in certain disclosure documents prepared by SDCWA. The SDCWA has entered into certain continuing disclosure agreements pursuant to which SDCWA is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 of the Exchange Act ("Rule 15c2-12") and annual audited financial statements (the "SDCWA Information") with the Municipal Securities Rulemaking Board which are available online at [www.emma.msrb.org](http://www.emma.msrb.org).

**SDCWA HAS NOT REVIEWED THIS REOFFERING MEMORANDUM AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO SDCWA. SDCWA IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH SDCWA INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

**MWD Water Supply.** The SDCWA currently purchases all of its imported water from MWD and IID. SDCWA is MWD's largest member agency, purchasing approximately [24%] of MWD's supplies in Fiscal Year 2009/10. MWD obtains its water supply from two primary sources: the Colorado River, via MWD's Colorado River Aqueduct, and the State of California Department of Water Resources' State Water Project ("SWP"), via the Edmund G. Brown California Aqueduct.

MWD faces various challenges in the continued supply of imported water to SDCWA and other member agencies. A description of these challenges as well as a variety of other operating information with respect to MWD is included in "APPENDIX F" hereto and in certain disclosure documents prepared by MWD. MWD has entered into certain continuing disclosure agreements pursuant to which MWD is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 and annual audited financial statements (the "MWD Information") with the Municipal Securities Rulemaking Board which are available online at [www.msrb.org](http://www.msrb.org).

**MWD HAS NOT REVIEWED THIS REOFFERING MEMORANDUM AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO MWD. MWD IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH MWD INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

**Historic and Projected Water Supply.** As noted, the State of California has experienced drought conditions for several years, which have impacted the SDCWA's base allocation of water to the District. The District's base allocation of potable water is 43,162 acre feet. In 2009, SDCWA implemented an 8% reduction in the base allocation to its customers, resulting in an allocation to the District of 39,680.6 acre feet. On April 28, 2011, SDCWA announced the end of mandatory water use restrictions and that there will no longer be a reduced water allocation for member agencies

At its peak in Fiscal Year 2006/07, the District purchased 41,909 acre feet of potable water from SDCWA. Of this amount, 3,073 acre feet of potable water was used to provide water to the customers of the District's recycled water system. However, the District has developed additional sources of recycled water and no longer needs to purchase potable water to supplement the recycled system. This has resulted in a reduction of purchased water from SDCWA from a high of 41,909 acre feet in Fiscal Year 2006/07 to 31,168 acre feet in Fiscal Year 2009/10, well below the current reduced allocation of 39,680.6 acre feet. Purchased water from SDCWA is expected to be maintained at approximately 21% below the reduced allocation and 26% below the District's projected highest demand year for the next several years.

Set forth below is a summary of the District's sources of water supply for the last eight Fiscal Years.

#### HISTORIC WATER SUPPLY IN ACRE-FEET PER YEAR

<b>Fiscal Year Ended June 30</b>	<b>Produced Recycled Water</b>	<b>Purchased Recycled Water</b>	<b>Purchased Potable Water</b>	<b>Total</b>
2003	1,117	0	34,539	35,656
2004	1,305	0	38,918	40,223
2005 <sup>(1)</sup>	1,150	0	37,678	38,828
2006	1,234	0	40,946	42,180
2007 <sup>(2)</sup>	1,263	653	41,909	43,825
2008	1,235	3,595	38,045	42,875
2009	844 <sup>(3)</sup>	3,686	34,971	39,501
2010	1,032	2,871	31,168	35,071

Source: Otay Water District.

<sup>(1)</sup> Rainfall in 2005 was significantly above average, resulting in decreased purchases of potable water and production of recycled water.

<sup>(2)</sup> After the District began purchasing recycled water from the City of San Diego in May of 2007, it was no longer necessary to purchase potable water for the recycled system to supplement the amount of produced recycled water. See "Water Supply - Service Area Water Supply - Recycled" above.

<sup>(3)</sup> The treatment plant was not in operation for a total of 74 days in Fiscal Year 2008/09 for planned maintenance.

The District currently expects that demand for potable water may reach as high as 60,000 acre feet per year at buildout, potentially by the year 2040. In order to provide enough water to meet expected demand at buildout, the District continues to develop additional sources of water.

Currently, the District is negotiating a long term purchase contract for potable desalinated water. The desalination plant, if constructed, would be located in Mexico. The plant is likely to take several years to complete, and is estimated to produce 100,000 acre feet of desalinated water annually. If constructed, it is expected that an approximate 24,000 acre feet of water could initially be supplied to the District from this source. This water supply would be delivered to the District's boundary coincident with the United States and Mexican international border. In order to take delivery of such water supply, the District needs to construct a conveyance system, within the District, from that delivery point to the District's distribution system. The construction includes 3.2 miles of pipeline, a pump station and a water treatment plant. The District expects that the conveyance system would take approximately 3 years to construct and the District would commence construction if a purchase contract is entered into.

As noted, the District is currently negotiating terms of the purchase contract, which may include a take-or-pay arrangement for all contracted water amounts. Water purchases under such a contract would be payable as an Operation and Maintenance Cost of the District, similar to the current water purchases from SDCWA and other existing sources. The District projects no appreciable difference in the cost of such water compared to current estimated costs of water purchased from SDCWA.

If the desalinization plant is completed, the District would expect to reduce the amount of water it purchases from SDCWA. However, should water from the desalinization plant be unavailable, as a member of SDCWA, the District would be entitled to request additional water purchases from SDCWA. The District believes that such a transition back to increased SDCWA water purchases could require temporary rate increases but would not have a material adverse effect on the District's financial condition.

The District makes no guarantee that the desalination plant will be constructed, and if so constructed, cannot guarantee construction in accordance with the timelines described herein. The District also provides no assurance that any contractual arrangement for the purchase of water from the facility will be executed with the terms described herein.

The District also continues to convert existing potable connections to the recycled water system when possible. In addition, the District anticipates converting a significant number of potable connections in the Otay Mesa area to the recycled system once the required pipelines are put in place, estimated to occur in four to five years.

Set forth below is a summary of the District's projection of water sources for the current and five succeeding Fiscal Years and includes desalinated water purchases in the "Purchased Potable Water" column beginning in 2013.

**PROJECTED WATER SUPPLY IN ACRE-FEET PER YEAR**

<b>Fiscal Year Ending June 30</b>	<b>Produced Recycled Water <sup>(1)</sup></b>	<b>Purchased Recycled Water</b>	<b>Purchased Potable Water <sup>(2)</sup></b>	<b>Total</b>
2011	1,202	2,946	30,142	34,290
2012	854 <sup>(3)</sup>	3,105	30,438	34,397
2013	1,100	3,041	30,971	35,112
2014	1,100	3,126	31,522	35,748
2015	1,100	3,156	31,897	36,153
2016	1,100	3,196	32,296	36,592

Source: Otay Water District.

<sup>(1)</sup> Maximum capacity for the treatment plant is 1,456 acre feet, but the District bases its projection of 1,100 acre feet on normal (efficient) capacity.

<sup>(2)</sup> Includes purchases from SDCWA, raw water treated to potable level by the City of San Diego and the Helix Water District, and assumes desalinated water purchases.

<sup>(3)</sup> In Fiscal Year 2012, the District plans work on the treatment plant, lowering production temporarily and increasing recycled purchases.

## Capital Improvement Program

The District boundaries encompass areas of San Diego County that experienced rapid growth between 2001 and 2007, and significant growth is expected in future years. The District currently serves a population of approximately 206,000. Ultimately, the District is projected to serve 277,000 people and it estimates an additional \$350 million investment in capital assets will be required through ultimate buildout, over 20 years.

The District has developed a six-year Capital Improvement Program (the “CIP”) based on future water demands in its Service Area. The District reviews and updates the CIP at least annually based on an analysis of the potable and recycled water demands most recently projected by developers, demographics, and population estimates by the San Diego Association of Governments. Major capital improvements within the next six years are planned in order to provide facilities to deliver water to new customers and to acquire additional water and recycled water capacity. These facilities are categorized by the District into those improvements relating to the Water System, which includes recycled water. Within each segregated operational area, the CIP is further separated into improvement categories – Expansion, Betterment and Replacement.

The table below summarizes the current six-year \$155 million Capital Improvement Program for the Water System and the categories of work to be completed.

	Fiscal Year Ending June 30						Total
	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	
Expansion	\$ 4,866,000	\$ 2,972,000	\$ 3,965,000	\$ 4,033,000	\$ 7,890,000	\$20,789,000	\$ 44,515,000
Betterment	6,472,000	4,585,000	9,279,000	5,970,000	9,420,000	11,700,000	47,426,000
Replacement	9,774,000	11,869,000	8,266,000	8,155,000	8,619,000	2,155,000	48,838,000
New Supply	<u>1,520,000</u>	<u>1,920,000</u>	<u>6,120,000</u>	<u>3,980,000</u>	<u>120,000</u>	<u>120,000</u>	<u>13,780,000</u>
Total	\$22,632,000	\$21,346,000	\$27,630,000	\$22,138,000	\$26,049,000	\$34,764,000	\$154,559,000

Source: Otay Water District.

The District has identified the timing and method of funding the capital improvements over the next six years. Each category of improvements is designed to be funded with operational net cashflow, bond proceeds, transfers between operational areas, other capital related charges, reserves or a combination of these sources. The District expects to fund these improvements with reserves, operating income, investment income, bond proceeds, capacity fees and other fees, grants and additional financing. The District expects that additional financing may occur in 2014. In order to implement the Capital Improvement Program, the District anticipates that it will need to increase its rates as described herein (see “Water Charges” herein). However, there is no guarantee that the District will implement such rate increases at the amount and at the time anticipated in its planning documents. See “Water Charges - Proposition 218.”

## Water Service

**Historical Water Use.** Table No. 1 shows the amount of water usage, connections and revenue generated from water and recycled water sales in the last five fiscal years, with estimated amounts for 2010/11. There have been over 1,639 new residential connections between Fiscal Years 2004/05 and 2010/11, an increase of 3%. Population has increased over 37% during this period from 148,000 to over 206,000, accounting for the significant increase in the amount of water usage.

Rainfall in Fiscal Year 2010/11 was above average and above recent years' totals. Together with conservation efforts by customers, this has caused a reduction in water sales in 2010/11 from amounts budgeted by the District. Historical rainfall totals are shown below.

### HISTORICAL RAINFALL

<b>Year</b>	<b>Inches</b>
2006	5.42
2007	3.85
2008	7.49
2009	9.17
2010	11.01
2011 (estimate)	12.27

**TABLE NO. 1**  
**CONNECTIONS AND WATER SALES VOLUME AND REVENUE**  
**Fiscal Years 2005/06 through 2010/11**

	<u>2005/06</u>	<u>2006/07</u>	<u>2007/08</u>	<u>2008/09</u>	<u>2009/10</u>	Estimate <u>2010/11</u> <sup>(5)</sup>
<u>Potable</u>						
Residential - Volume in ccf <sup>(1)</sup>	9,228,713	9,713,112	9,402,189	8,881,191	7,690,856	7,504,151
- Volume in acre feet	21,185	22,298	21,583	20,387	17,652	17,227
Residential - Connections	42,763	43,292	43,342	43,431	43,619	43,849
Residential - Sales Revenue <sup>(2)</sup>	\$ 16,784	\$ 18,695	\$ 17,775	\$ 17,853	\$ 18,389	\$ 19,587
All Others - Volume in ccf	5,875,415	6,346,352	6,173,480	6,042,570	5,058,943	4,811,821
- Volume in acre feet	13,487	14,568	14,171	13,871	11,611	11,046
All Others - Connections	4,088	4,168	4,249	4,257	4,227	4,252
All Others - Sales Revenue <sup>(2)</sup>	\$ 11,191	\$ 12,002	\$ 12,261	\$ 12,523	\$ 12,979	\$ 12,506
Total Potable Connections	46,851	47,460	47,591	47,688	47,846	48,101
Annual Increase In Connections	809	609	131	97	158	255
<u>Recycled</u> <sup>(3)</sup>						
Recycled - Volume in ccf	1,729,000	1,920,287	2,001,137	1,991,682	1,774,563	1,662,529
- Volume in acre feet	3,969	4,408	4,594	4,572	4,073	3,817
Recycled - Connections	558	588	626	671	681	681
Recycled - Sales Revenue <sup>(2)</sup>	\$ 3,066	\$ 3,886	\$ 5,182	\$ 5,499	\$ 6,002	\$ 6,200
Annual Increase in Connections	75	30	38	45	10	0
<u>Total</u>						
Total Volume in ccf	16,830,128	17,979,751	17,576,806	16,915,448	14,524,362	13,978,501
Total Volume in acre feet	38,641	41,274	40,348	38,830	33,336	32,089
Total Connections	47,409	48,048	48,217	48,359	48,527	48,782
Total Sales Revenue <sup>(2)</sup>	\$ 31,041	\$ 34,583	\$ 35,218	\$ 35,875	\$ 37,370	\$ 38,293
Fixed Charges <sup>(4)</sup>	\$ 12,715	\$ 14,023	\$ 15,535	\$ 16,524	\$ 18,840	\$ 19,906
Total Revenue	\$ 43,756	\$ 48,606	\$ 50,753	\$ 52,399	\$ 56,210	\$ 58,199

Source: Otay Water District.

<sup>(1)</sup> ccf refers to a measurement of 100 cubic feet (1 cubic foot = 7.48 gallons).

<sup>(2)</sup> Revenue in \$ Thousands.

<sup>(3)</sup> The District receives a credit from SDCWA and MWD for every acre-foot of recycled water sold. Beginning in May 2007, the District stopped purchasing potable water to supplement the recycled water purchases for the recycled system and since that time the credit has been received on all recycled water sold, and is included in Recycled Sale Revenue.

<sup>(4)</sup> Includes fixed charges, energy charges and delinquency collections on both potable and recycled water sales.

<sup>(5)</sup> The District projects that actual potable sales volume in 2010/11 will be 6% less than budgeted, and actual recycled water sales volume will be 12% less than budgeted. This is a result of above average rainfall, below average temperatures and continued conservation efforts of customers. See "Projected Debt Service Coverage" herein.

Table No. 2 shows the 10 largest water users for Fiscal Year 2009/10.

**TABLE NO. 2**  
**TEN LARGEST CUSTOMERS BY WATER SALES REVENUES <sup>(1)</sup>**  
**Year ended June 30, 2010**

<u>Customer</u>	<u>Business Type</u>	Usage in Hundred <u>Cubic Feet</u>	Usage in <u>Acre Feet</u>	% of Water System <u>Consumption</u>	<u>Water Sales</u> <u>Revenues</u>	% of Total Water Sales <u>Revenues</u>
City of Chula Vista	Public	646,549	1,484	4.5%	\$2,218,584	3.9%
County of San Diego	Public <sup>(2)</sup>	280,563	644	1.6	943,132	1.7
State of California	Public <sup>(3)</sup>	292,077	671	1.6	803,450	1.4
Eastlake III Community Association	Construction/ Irrigation <sup>(4)</sup>	172,267	395	1.0	531,489	0.9
Eastlake Summit Association	Construction	46,898	108	0.3	523,703	0.9
Eastlake Country Club	Irrigation <sup>(4)</sup>	150,809	346	0.8	406,813	0.7
Belleme HOA	Irrigation <sup>(4)</sup>	47,209	108	0.3	397,621	0.7
Chula Vista School District	Public	105,524	243	0.6	377,411	0.7
Cuyamaca College	Public	41,612	96	0.2	354,666	0.6
Sweetwater School District	Public	<u>105,931</u>	<u>243</u>	<u>0.6</u>	<u>348,083</u>	<u>0.6</u>
		1,889,439	4,338	10.5%	\$6,904,952	12.3%

Source: Otay Water District.

<sup>(1)</sup> Includes both potable and recycled water sales and excludes fixed charges.

<sup>(2)</sup> George F. Bailey Detention Facility.

<sup>(3)</sup> Richard J. Donovan Correctional Facility.

<sup>(4)</sup> Recycled water use.

## Water Charges

**Water Service Rates.** The District held a public hearing on August 24, 2009 and approved a five-year schedule of rates, which included authorization to raise rates by up to 10% per year during the five year period for costs other than SDCWA, San Diego and MWD rate increases and to pass through all SDCWA, San Diego and MWD increases without limitation during the five year period. A 19.9% rate increase took effect for water usage beginning September 1, 2009 and a 10.9% rate increase took effect for water usage beginning January 1, 2011. The Board of Directors will continue to take action each year to set rates, however they are not expected to need to hold another Proposition 218 hearing for three more years. See "Proposition 218" below.

The District, based on its internal rate model and the need to fund the CIP, increased rates by 7.7% for water usage beginning January 1, 2012. The District anticipates that it will need to increase its rates by approximately 7.7% in each of the next three years and 4.9% in each of the following three years. The largest component of the required rate increases is related to the increase in purchased water costs from SDCWA. For Fiscal Year 2011/12, the expected cost increase provided by SDCWA is greater than the projected the 7.7% estimated rate increase by the District.

The water rate structure uses both fixed and variable charges. All customer classes are charged the “monthly fixed charge” based on the meter size as shown in Table No. 3. The commodity or consumption rates as outlined in Table No. 4 are variable in that they are charges per unit. The District also uses an inclining block rate structure for the commodity rate. As a result, each class of customer has a range of rates and for certain classes - commercial, irrigation, and recycled - rates are further differentiated based on meter size. Residential customers (also called domestic customers) have a range of rates beginning at \$2.10 and up to \$4.21 based on the number of units used. The average residential customer uses 15 units of water. One unit of water is equal to 100 cubic feet of water (one cubic foot of water equals 7.48 gallons). Customers outside the District and tanker trucks are charged two times the commodity rate.

**TABLE NO. 3**  
**MONTHLY FIXED CHARGES**  
**As of January 1, 2011**

<u>Meter Size</u>	Domestic Service Monthly <u>Fixed Charge</u>	MWD/SDCWA Additional Monthly <u>Fixed Charge</u>
3/4"	\$ 14.58	\$ 11.82
1"	18.52	19.69
1-1/2"	28.37	39.49
2"	40.18	63.07
3"	71.68	126.14
4"	107.13	197.11
6"	205.59	394.17
8"	323.73	630.71
10"	461.57	903.58
Fire	30.11	

Source: Otay Water District.

**TABLE NO. 4  
COMMODITY RATES  
As of January 1, 2011**

<u>Customer Class: Domestic</u>		<u>Customer Class: Master Meter</u>	
<u>Units <sup>(1)</sup></u>	<u>Charge Per Unit</u>	<u>Units <sup>(1)</sup></u>	<u>Charge Per Unit</u>
Lifeline ( Less than 5 hcf)	\$1.49	0-4	\$2.29
6-10	2.31	5-9	2.97
11-22	3.00	Over 9	4.57
Over 23 hcf	4.63		

\* Note: Customers whose total consumption is 10 units or less per month shall receive a benefit of a lower rate for units 1-5. These units will be billed at a rate of \$1.49 per unit.

<u>Customer Class: Commercial</u>		
<u>Less Than 10" Meter:</u>	<u>10" Meter or Greater:</u>	<u>Charge Per Unit</u>
0-173 Units	0-7,426 Units	\$2.44
174-831 Units	7,427-14,616 Units	2.50
Over 832 hcf Units	Over 14,617 Units	2.54

<u>Customer Class: Irrigation</u>			
<u>3/4"-1" inch Meter:</u>	<u>1-1/2"-2" Meter:</u>	<u>3" and Up Meter:</u>	<u>Charge Per Unit</u>
0-49 Units	0-144 Units	0-1,044 Units	\$3.32
50-132 Units	145-355 Units	1,045-8,067 Units	3.39
Over 133 hcf Units	Over 356 hcf Units	Over 8,068 hcf Units	3.45

<u>Customer Class: Recycled</u>				
<u>3/4"-1" Meter:</u>	<u>1-1/2"-2" Meter:</u>	<u>3"-4" Meter:</u>	<u>6" Meter or Greater:</u>	<u>Charge Per Unit</u>
0-42 Units	0-168 Units	0-403 Units	0-7,916	\$2.84
43-97 Units	169-402 Units	404-820 Units	7,917-16,357	2.88
Over 98 Units	Over 403 Units	Over 821 Units	Over 16,358	2.94

Source: Otay Water District.

<sup>(1)</sup> 1 unit equals 100 cubic feet of water.

Additionally, commercial agriculture users participating in MWD or SDCWA conservation programs are eligible to receive discounts from the base agriculture rate. As noted above, the District has estimated that future rate increases will be necessary to implement the current six-year CIP. Additionally, the rates, charges and fees may be increased each year to pass-through increases in costs imposed by SDCWA, San Diego or MWD not already estimated to occur (approximately 89% of the projected rate increases over the next five years relate to estimated increases in SDCWA and MWD charges to the District).

Table No. 5 compares average residential water rates charged by the District with surrounding cities and other water agencies in San Diego County.

**TABLE NO. 5  
COMPARISON OF  
PROPOSED RESIDENTIAL WATER RATES  
As of March 1, 2011**

<u>City/Water Agency</u>	<u>Average Rates <sup>(1)</sup></u>
Lakeside	\$58.28
Oceanside	64.35
Helix WD	64.65
Poway	66.05
Olivenhain Water District	66.95
Yuima Water District	68.17
<b>Otay Water District</b>	<b>69.22</b>
San Dieguito Water District	69.71
San Diego	76.44
Carlsbad	76.74
Vallecitos Water District	77.19
Santa Fe	77.32
Valley Center	78.18
Escondido	79.28
Vista	79.64
Sweetwater Water District	80.86
Ramona	81.47
Padre Dam Water District - East	82.89
Padre Dam Water District - West	83.16
Rincon	87.91
Fallbrook	91.57
Del Mar	95.05
Rainbow Water District	97.48

Source: Otay Water District.

<sup>(1)</sup> Average rates based on assumed residential use of 15 ccf of water monthly.

**Delinquencies.** Accounts receivable that have not been paid in over 60 days represent less than 0.6% of the District's annual sales for the last three fiscal years. Accounts receivable between 30 to 60 days delinquent in payment have averaged 0.9% of the District's annual water sales for the last two fiscal years. In the last three fiscal years, the District has written off less than \$200,000 a year in uncollectible accounts.

The District has implemented a number of changes over the past few years which are significant in improving the management of the accounts receivables. The collection process is more efficient with the introduction of automatic dialers making it possible to address collections of smaller balances. The District has improved the collection process related to properties in foreclosure by collecting deposits and locking all vacant properties. The District has also provided new convenient payment options by introducing payments by phone and web. The District has increased the availability of account information by introducing 24/7 Interactive Voice Response. In addition, with the improvements in online banking systems, the turnaround time on payment processing has decreased from 10 to 2 days. These improvements implemented over the last few years have all assisted the District in better managing

its accounts receivable. The District continues to be focused on finding new ways to assist customers in managing their accounts. Some of the improvements currently being implemented are electronic bill presentation, recurring payments via credit card, and the ability to make water payments at any retailer using the same electronic network used by the District's bank.

**Other Charges.** The District charges an energy charge of \$0.044 per 100 feet of elevation for all connections over a 450 foot elevation. Betterment charges in certain areas ranging from \$.08 to \$.27 per unit to pay for reservoirs, pump stations and other infrastructure. The District also applies additional water development charges in some areas in the North District.

**Capacity Fees and Meter Fees.** The District charges capacity fees to connect to the Water System. Current capacity fees are \$7,697 and the new water supply of \$887 for a single family residential connection, increased quarterly according to the Engineering News-Record index. The District also charges a meter fee for the materials and installation cost of a meter. The meter fees range from \$266 for a single family residence to \$5,507 for a 10" meter.

**Availability Fees.** The District levies and collects annual standby availability charges. Current legislation provides that any availability charge in excess of \$10 per acre shall be used only for the purpose of the improvement district for which it was assessed. Therefore, availability fees shown in Table No. 9 and Table No. 10 include only the first \$10 of availability fees. To the extent the availability fees in excess of \$10 per acre are authorized for operational purposes, they are included in Table No. 9 in "Connection and Other Fees" and in Table No. 10 in "Other Income."

**Annexation Fees.** When service is requested outside the boundaries of the District, the land to be serviced is annexed and an annexation fee is charged by the District. Current annexation fees are \$1,516 for single family residential connections and are adjusted quarterly according to the Engineering News-Record index.

Annexation fees are currently charged for new service that may be within the District boundaries, but outside of an improvement district within the District boundaries. The new annexation fees are expected to apply only to properties outside the District boundaries.

As a result of the change in fee structure, future capacity fees and annexation fees may not be comparable to amounts shown in prior years.

**Proposition 218.** On November 5, 1996, California voters approved Proposition 218, the "Right to Vote on Taxes Act." Proposition 218 added Articles XIIC and XIID to the State Constitution, which contain a number of provisions affecting the ability of the District to levy and collect both existing and future taxes, assessments, fees and charges. Proposition 218 also extends the initiative power to reducing or repealing any local taxes, assessments, fees and charges. This extension of the initiative power is not limited to taxes, assessments, fees and charges imposed on or after November 6, 1996, the effective date of Proposition 218, and could result in retroactive repeal or reduction in any existing taxes, assessments, fees or charges, except those which are pledged to the repayment of debt. If such provisions were held to apply to the District's fees or charges and a repeal or reduction in District fees or charges were to occur, and it was held that any such taxes, assessments, fees or charges were not pledged to any debt repayment, the District's ability to pay debt service on the Bonds could be adversely affected. It is also possible that the courts would uphold a reduction in rates and charges that reduce the coverage available from Net Revenues below the levels historically maintained by the District.

Article XIID conditions the imposition or increase of any "fee" or "charge" upon there being no written majority protest after a required public hearing and, for fees and charges other than for sewer, water or refuse collection services, voter approval. Article XIID defines "fee" or "charge" to mean levies (other than *ad valorem* or special taxes or assessments) imposed by a local government upon a parcel or upon a person as an incident of the ownership or tenancy of real property, including a user fee or charge for a

“property-related service.” One of the requirements of Article XIIIID is that before a property related fee or charge may be imposed or increased, a public hearing upon the proposed fee or charge must be held and a mailed notice sent to the record owner of each identified parcel of land upon which the fee or charge is proposed for imposition. In the public hearing if written protests of the proposed fee or charge are presented by a majority of the owners of affected identified parcel(s), an agency may not impose the fee or charge.

Following the enactment of Proposition 218 in 1996, appellate court cases and an Attorney General opinion initially indicated that fees and charges levied for water and wastewater services are not property-related fees and charges and thus are not subject to the above described requirements of Proposition 218 regarding notice, hearing and protests in connection with any increase in the fees and charges being imposed.

In a decision rendered in February, 2004, the California Supreme Court in *Richmond et al. v. Shasta Community Services District*, 32 Cal. 4th 409, upheld a Court of Appeals decision that water and wastewater connection fees were not property related fees or charges subject to Article XIIIID, while at the same time stating in dicta that fees for ongoing water and wastewater service through an existing connection were property related fees and charges.

On March 23, 2005, the California Fifth District Court of Appeal published *Howard Jarvis Taxpayers Association v. City of Fresno*, concluding that in lieu fees charged as a component of water and wastewater utility service charges are subject to the requirements of Proposition 218. The ruling in the *City of Fresno* case relied in part on the *Richmond* decision’s dicta and appeared to conflict with *Apartment Association of Los Angeles County, Inc. v. City of Los Angeles*, 24 Cal. 4th 830 (2001), in which the California Supreme Court ruled that the property-related fee provisions of Proposition 218 apply only to fees triggered by property ownership alone and not by voluntary conduct of the property owner, such as consuming utility services. The *City of Fresno* decision is final, as review has been denied by the California Supreme Court.

On July 24, 2006, the California Supreme Court stated in *Bighorn-Desert View Water Agency v. Beringson* that charges for ongoing water delivery are property related fees and charges within the meaning of Article XIIIID and are further subject to the initiative provisions of Section 3 of Article XIIIIC. This decision reversed the July 2004 California Appellate Court decision (*Bighorn-Desert View Water Agency v. Beringson* (180 Cal. App 4<sup>th</sup> 890)) which opined that the costs of water services are not property related or incidents of property ownership because they are based on consumption and not on property ownership. The California Supreme Court held that such water service charges may be reduced or repealed through a local voter initiative pursuant to Article XIIIIC of the California Constitution. The Supreme Court stated that it was not holding that the initiative power is free of all limitations and was not determining whether the initiative power is subject to the statutory provision requiring that water service charges be set at a level that will pay debt service on bonded debt and operating expenses. However, the Supreme Court stated in its opinion that water providers may determine rates and charges upon proper action by the governing body and that the legislative body may increase a charge which was not affected by initiative or impose an entirely new charge.

As a result of this case, there can be no assurance that Proposition 218 will not limit the ability of the District to impose, levy, charge and collect increased fees and charges for water services.

On August 24, 2009, the District approved rate increases effective for water usage beginning September 1, 2009 following mailing of notice and a public hearing held pursuant to Article XIIIID of the Constitution. This approval includes authorization to raise rates by up to 10% per year for the next five years for costs other than SDCWA and MWD rate increases. The approval includes authorization to pass through all such SDCWA and MWD increases without limitation during the five year period. The Board of Directors will continue to take action each year to set rates, however they are not expected to need to hold another Proposition 218 hearing for three years.

## Taxes

The County levies a 1% *ad valorem* tax on behalf of all taxing agencies in the County, including the District. For Fiscal Year 2010/11, the District's share of such property tax is projected to be \$3.15 million, representing an increase of \$56,000 from amounts received in 2009/10. Such taxes are a source of payment for the Installment Payments. See "SOURCES OF PAYMENT FOR THE BONDS - Installment Payments." All property is assessed using full cash value as defined by Article XIII A of the State Constitution. State law provides exemptions from *ad valorem* property taxation for certain classes of property such as churches, colleges, non-profit hospitals and charitable institutions.

The taxes collected are allocated to taxing agencies within the County, including the District, on the basis of a formula established by State law enacted in 1979 and modified from time to time. Under this formula, the County and all other taxing entities receive a base year allocation plus an allocation on the basis of "situs" growth in assessed value (due to new construction, change of ownership, or a 2% inflation allowance allowed under Article XIII A of the State Constitution) prorated among the jurisdictions which serve the tax rate area within which the growth occurs. Tax rate areas are groups of parcels which are taxed by the same taxing entities. Cities, counties, special districts and school districts share the growth of "base" revenues from each tax rate area. Assessed valuation growth is cumulative, i.e., each year's growth in property value becomes part of each District's allocation in the following year.

Historical assessed valuations for the District may be found in the District's Comprehensive Annual Financial Report, attached hereto as "APPENDIX B." Over the last 30 months, the severe economic recession reverberated through the residential housing market in the County, including many portions of the District and particularly the area in Chula Vista. Between 2008/09 and 2010/11, the assessed valuation of property city-wide in Chula Vista declined 10.4%. The County Assessor reports that the County reduced the value of 225,000 properties throughout the County in 2009, with an average reduction of \$112,000 for a single family home. Foreclosure rates have also increased significantly in the County in the last 36 months. The District's estimate of Taxes for 2010/11 reflects these reduced assessed values.

The availability of revenue from growth in the tax base may be affected by the establishment of redevelopment agencies which, under certain circumstances, may be entitled to revenues resulting from the increase in certain property values. As of the date of this Reoffering Memorandum, a portion of the District's tax base is within a redevelopment plan area.

California law exempts \$7,000 of the assessed valuation of an owner-occupied dwelling but this exemption does not result in any loss of revenue to local agencies since an amount equivalent to the taxes which would have been payable on such exempt values is made up by the State.

Under AB 454 (Statutes of 1987, Chapter 921), the State reports to each county auditor-controller only the county-wide unitary taxable value of State-assessed utility property, without an indication of the distribution of the value among tax rate areas. The provisions of AB 454 apply to all State-assessed property except railroads and non-unitary properties, and do not constitute an elimination of a revision of the method of assessing utilities by the State Board of Equalization. AB 454 allows generally valuation growth or decline of State-assessed unitary property to be shared by all jurisdictions within a county.

From time to time, legislation has been considered as part of the State budget to shift the share of the 1% *ad valorem* property tax collected by counties from special districts to school districts or other governmental entities (the "ERAF Shift"). While legislation enacted in connection with the Fiscal Year 1992/93 State budget shifted approximately 35% of many special districts' shares of the countywide 1% *ad valorem* tax, the share of the countywide 1% *ad valorem* tax pledged to debt service by special districts was exempted. None of the State budgets enacted since Fiscal Year 1992/93 have permanently reallocated additional portions of the special districts' shares of the countywide 1% *ad valorem* tax.

However, the State Budgets for Fiscal Years 2003/04 through 2005/06 reallocated approximately \$1.30 billion of the 1% *ad valorem* property tax from local government to schools. Of that amount, approximately \$350 million was reallocated from special districts. The District estimates that this resulted in a reduction of approximately 40% in Taxes as a result of the ERAF Shift in those years. On July 24, 2009, the California legislature approved amendments to the 2009/10 Budget involving 30 separate pieces of legislation to close a \$26.3 billion shortfall. The Governor signed the budget plan on July 28, 2009. Total State general fund spending in Fiscal Year 2009/10 will be more than \$84 billion, down from nearly \$91.7 billion in Fiscal Year 2008/09 and nearly \$103 billion in Fiscal Year 2007/08. The budget amendments combined deep spending cuts, borrowing from local governments and accounting maneuvers.

The approved amendments included borrowing from local governments and various accounting maneuvers to generate additional revenues in Fiscal Year 2009/10, including (among many others) \$2 billion borrowed from cities, counties and special districts' property tax collections under provisions of Proposition 1A (approved by the voters in 2004), which the State must repay with interest within three years.

The declaration by the State of California of a fiscal emergency under Proposition 1A, as a part of the State's 2009/10 budget adoption, authorized the State to withhold the equivalent of 8% of fiscal 2009/10 property related tax revenues from cities, counties and special districts. The tax revenues are required to be repaid by the State with interest within three years. The District's Proposition 1A receivable was \$267,197. As a part of the budget package, local governments were given the opportunity to sell their Proposition 1A receivable through financing offered by the California Statewide Communities Development Authority, a joint powers authority sponsored by the League of California Cities and California State Association of Counties. California Communities issued bonds in November 2009, securitizing the future payments by the State and remitting the proceeds of the bonds to the local governments who opted to participate in the securitization. The District opted to participate in the securitization program and received all of its Proposition 1A receivable.

There can be no assurance that the share of the 1% *ad valorem* property tax the District currently receives will not be reduced further or deferred or delayed pursuant to State legislation enacted in the future to address future State budget deficits. See "Historical and Projected Taxes, Net Revenues and Debt Service Coverage" herein for historic and projected receipts of Taxes.

## **Personnel**

The District has 156 full-time positions budgeted for Fiscal Year 2011/12. The OWD Employee Association (the "Union") represents 115 of these full-time employees as a collective bargaining unit. The District has not experienced any strikes and continues to have positive labor relations which includes a negotiated five-year Collective Bargaining Agreement that ends on June 30, 2013.

The District provides retirement benefits for its employees through a contractual agreement with the California Public Employees' Retirement System ("CalPERS"). Active members in the District's benefit pension plan are required to contribute 8% of their annual covered salary. The District has elected to contribute 7% on behalf of its employees. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the Fiscal Year ended June 30, 2010 was 19.815%. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. Due to significant investment losses, CalPERS could significantly increase contribution rates over the next several years. For the Fiscal Year ended June 30, 2010, the District's annual pension costs and actual contribution was \$2,240,538, and, for the Fiscal Year ending June 30, 2011, the District's annual pension cost and actual contribution is expected to be \$2,427,744, an 8.4% increase. An increase of 14.3% is expected for 2011/12 and a 2.4% increase is expected for

2012/13. The required contribution for Fiscal Year 2010/11 was determined as part of the June 30, 2008 actuarial valuation, pursuant to which the District had an unfunded actuarial accrued liability of approximately \$15.8 million as of June 30, 2008. As part of the June 30, 2009 actuarial valuation, CalPERS estimates the District's unfunded actuarial accrued liability will not change significantly as of June 30, 2010 or June 30, 2011. Unfunded liabilities are amortized as a level percentage of pay over a closed 20-year period. Gains and losses that occur in the operation of the plan are amortized over a rolling period, which results in an amortization of 10% of unamortized gains and losses each year. If the plan's accrued liability exceeds the actuarial value of plan assets, then the amortization payment of the total unfunded liability may not be lower than the payment calculated over a 30-year amortization period.

In addition to the pension benefits described above, it is the District's practice and policy to provide certain life insurance and health care benefits ("Other Post Employment Benefits, or OPEB") for eligible retired employees, directors and eligible dependents. These benefits vary based on the hire date of the employee. As of the last actuarial projection, dated June 30, 2009, the District's Actuarial Accrued Liability for OPEB benefits was \$10,070,000.

The District has chosen to fund this liability by investing funds with the California Employers' Retiree Benefit Trust Fund (CERBT), an agent multiple-employer plan administered by California Public Employees' Retirement System (CalPERS), which acts as a common investment and administrative agent for participating public employers within the State of California. The District's annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal annual cost. Any unfunded actuarial liability (or funding excess) is amortized over a period not to exceed thirty years. The current ARC rate is 2.3% of the annual covered payroll.

Based on the District's financial statements at June 30, 2010, the amount actually contributed to the CERBT and changes in the District's net OPEB obligation total \$6.8 million. In addition, the District's Board has designated approximately \$3.0 million of its reserves towards the remaining liabilities. In accordance with GASB Statement 45, and the requirements of the CERBT, the District will periodically update the actuarial projections and continue to fund the resulting ARC on an annual basis.

## **Insurance**

### General Liability and Property Damage

The District is exposed to various risks of loss related to torts, theft, damage and destruction of assets, errors and omissions, and natural disasters. Beginning in July 2003, the District began participation in an insurance pool through Special Districts Risk Management Authority (SDRMA). Coverages through SDRMA are as follows: property coverage - \$1 billion/occurrence with replacement cost for scheduled property; \$100 million for boiler and machinery; \$200 million for workers' comp.; \$500,000 for personal liability coverage for board members; \$400,000 for employee dishonesty coverage; \$750,000 for uninsured/underinsured motorists; and \$10 million per occurrence for each of the following types of coverage, auto liability, public officials and employees errors, employment practices liability, employee benefits liability, and general liability.

Separate financial statements for SDRMA may be obtained at: Special District Risk Management Authority, 1112 I Street, Suite 300, Sacramento, California 95814.

### Workers' Compensation

Through SDRMA, the District is insured up to \$200 million Statutory Workers' Compensation and \$5 million in Employer's Liability with a Zero Member Deductible. SDRMA currently has a pool of over 340 agencies in the Workers' Compensation Program.

## Health insurance

Prior to 2008, the District maintained a self-insurance program for health claims. Beginning in January 2008, the District began providing health insurance through SDRMA covering all of its employees, retirees, and other dependents. Prior estimated accrued claims outstanding at June 30, 2008 amounted to \$137,029, and all remaining claims were paid as of December 31, 2008. SDRMA is a self-funded pooled medical program administered in conjunction with the California State Association of Counties (CSAC).

## **District Reserves and Investment Policy**

As of June 30, 2010, the District had approximately \$115.3 million in cash and investments, of which the Board had designated \$52.2 million for capital projects and \$6.6 million for insurance. The District's reserves are not pledged to and do not secure the District's obligation to make Installment Payments.

In accordance with State of California law, the District Board of Directors has approved an investment policy (the "Investment Policy") which complies with Sections 53601 through 53630 of the Government Code of the State of California providing legal authorization for the investment or deposit of funds of local agencies. All investments of the District conform to the restrictions of those laws. The District's investments by category and their respective market value and book value as of March 31, 2011 are set forth in Table 5 below. For additional information relating to the District's investments, see "APPENDIX B - DISTRICT AUDITED FINANCIAL STATEMENTS," Note 2.

**TABLE NO. 6**  
**SUMMARY OF INVESTMENTS**  
**As of March 31, 2011**

<u>Investments</u>	<u>Market Value</u>	<u>Book Value</u>	<u>% of Portfolio</u>
Federal Agency Issues – Callable	\$66,279,429	\$66,365,240	66.15
Federal Agency Issues – Coupon	-	-	-
Certificates of Deposit – Bank	79,108	79,108	0.07
Local Agency Investment Fund (LAIF)	20,271,906	20,246,352	20.18
San Diego County Pool	12,010,000	11,986,744	11.95

Source: Otay Water District.

The Investment Policy may be changed at any time at the discretion of the District (subject to the State law provisions relating to authorized investments) and as the California Government Code is amended. Any exception to the Investment Policy must, however, be formally approved by the Board of Directors of the District. There can be no assurance the State law or the Investment Policy will not be amended in the future to allow for investments which are currently not permitted under such State law or the Investment Policy, or that the objectives of the District with respect to investments will not change.

## Outstanding Indebtedness of the District

The District had outstanding indebtedness as of June 30, 2010 as shown in Table No. 7.

**TABLE NO. 7**  
**OTAY WATER DISTRICT**  
**OUTSTANDING INDEBTEDNESS**  
**As of June 30, 2010**

Category of Indebtedness	Original Issue	Amount Outstanding	Final Maturity
(1) 1996 Certificates of Participation	\$15,400,000	\$11,700,000	2026
(2) 2004 Refunding Certificates of Participation	12,270,000	9,790,000	2023
(3) 2007 Certificates of Participation	42,000,000	40,400,000	2036
(4) 2009 General Obligation Refunding Bonds	7,780,000	7,780,000	2023
(5) State Water Resources Control Board Note	5,000,000	359,744	2011
(6) 2010 Water Revenue Bonds Series A	13,840,000	13,840,000	2025
(6) 2010 Water Revenue Bonds Series B	36,355,000	36,355,000	2041

- (1) In June 1996, the District issued the 1996 Certificates to provide funds for the design, acquisition, construction and equipping of various water and water-related facilities and an administration building for use in connection with the administration of the District. The 1996 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 2004 Certificates, the 2007 Certificates, and the 2010 Bonds. Interest is payable at a variable rate of interest, and the interest rate at April 19, 2011 was 0.26% and was 0.25% at June 30, 2010. At current rates, debt service is expected to be \$400,000 to \$450,000 each year for the next several years. However, the annual installment payments are estimated in the projections at approximately \$980,000 based on the current 25-Year Revenue Bond Index of 4.99%.
- (2) In August 2004, the District issued its 2004 Revenue Refunding Certificates of Participation (the "2004 Certificates") to defease its outstanding 1993 Certificates of Participation. The 2004 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$933,000.
- (3) In March 2007, the District issued its 2007 Revenue Certificates of Participation (the "2007 Certificates") to provide funds for the design, construction and equipping of two 10 million gallon reservoirs and various water-related facilities. The 2007 Certificates are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$2,501,000.
- (4) Voters within Improvement District No. 27 of the District authorized \$100 million general obligation bonds in 1989. The District issued \$11,500,000 general obligation bonds in 1992 and refinanced the bonds in 1998 and again in 2009. Annual debt service is approximately \$764,000. The District also has approximately \$29 million in general obligation bonds authorized between 1960 and 1978 for various Improvement Districts throughout the District, but unissued. The general obligation bonds are payable from *ad valorem* property tax revenues, which are not a part

of Taxes which secure the Installment Payments. The District has no current plans to issue any of the authorized but unissued general obligation bonds.

- (5) The State Water Resources Control Board Note bears interest at 3.5% and is payable in annual installments of \$366,325. This note has no lien on Net Revenues and Taxes but is payable by the District from any available source.
- (6) In April 2010, Water Revenue Bonds Series 2010A and Water Revenue Bond Series 2010B (Taxable Build America Bonds) (collectively, the “2010 Bonds”) were sold by the Otay Water District Financing Authority to provide funds for the construction of water storage and transmission facilities. The 2010 Bonds are payable from Installment Payments which are secured by a pledge of and lien on Net Revenues and Taxes on a parity with the Installment Payments securing the 1996 Certificates. Annual installment payments are approximately \$3,700,000.

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Source: Otay Water District.

## Historical Operating Results

The following table summarizes the Statement of Net Assets included in the District's audited financial statements for the last five Fiscal Years. The audited financial statements of the District for the Fiscal Year ended June 30, 2010 are attached hereto as "APPENDIX B" and should be read in their entirety.

**TABLE NO. 8**  
**OTAY WATER DISTRICT**  
**NET ASSETS**  
**For the Fiscal Year Ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
<b>ASSETS</b>					
Current Assets:					
Cash and Cash Equivalents	\$ 13,755,907	\$ 8,048,633	\$ 23,351,911	\$ 50,823,237	\$ 40,180,519
Restricted Cash and Cash Equivalents	-	11,191,213	3,753,983	1,760,631	21,131,924
Investments	62,596,513	68,912,864	60,682,507	26,169,080	43,085,300
Restricted Investments	-	19,975,538	-	-	11,150,549
Accounts Receivable	6,808,999	8,675,458	7,689,720	8,029,609	8,959,367
Accrued Interest Receivable	818,798	1,559,081	715,900	319,186	239,355
Taxes and Availability Charges Receivable	-	-	362,976	413,000	366,535
Restricted Taxes and Availability Charges Receivable	318,090	443,854	174,219	190,151	186,813
Inventories	592,426	633,697	711,240	816,865	954,007
Prepaid Expenses and Other Current Assets	<u>664,133</u>	<u>1,164,300</u>	<u>1,908,028</u>	<u>976,045</u>	<u>626,421</u>
Total Current Assets	<u>\$ 85,554,866</u>	<u>\$120,604,638</u>	<u>\$ 99,350,484</u>	<u>\$ 89,497,804</u>	<u>\$126,880,790</u>
Non-Current Assets:					
Restricted Assets:					
Net OPEB Obligation	\$ -	\$ -	\$ 5,649,008	\$ 6,204,876	\$ 6,783,385
Total Restricted Assets	\$ -	\$ -	\$ 5,649,008	\$ 6,204,876	\$ 6,783,385
Deferred Bond Issuance Costs	\$ 555,550	\$ 1,254,821	\$ 1,240,166	\$ 1,142,762	\$ 1,703,282
Capital Assets:					
Land	\$ 12,494,062	\$ 12,971,479	\$ 13,025,364	\$ 13,402,840	\$ 13,620,963
Construction in Progress	58,869,241	40,300,055	42,338,220	18,280,278	37,081,849
Capital Assets, Net of Depreciation	<u>325,624,281</u>	<u>370,989,434</u>	<u>391,350,813</u>	<u>422,369,157</u>	<u>420,363,833</u>
Total Capital Assets, Net of Depreciation	<u>\$396,987,584</u>	<u>\$424,260,968</u>	<u>\$446,714,397</u>	<u>\$454,052,275</u>	<u>\$471,066,645</u>
Other Non-Current Assets	<u>283,440</u>	<u>235,694</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total Non-Current Assets	<u>\$397,826,574</u>	<u>\$425,751,483</u>	<u>\$453,603,571</u>	<u>\$461,399,913</u>	<u>\$479,553,312</u>
Total Assets	<u>\$483,381,440</u>	<u>\$546,356,121</u>	<u>\$552,954,055</u>	<u>\$550,897,717</u>	<u>\$606,434,102</u>

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**NET ASSETS**  
**For the Fiscal Year Ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
<b>LIABILITIES</b>					
Current Liabilities:					
Current Maturities of Long-term Debt	\$ 1,529,848	\$ 1,519,048	\$ 2,445,214	\$ 2,521,772	\$ 2,668,734
Accounts Payable	11,617,499	10,930,658	13,705,566	11,565,953	15,327,365
Accrued Payroll Liabilities	2,348,853	2,270,958	2,491,182	2,548,731	2,743,408
Other Accrued Liabilities	683,350	1,597,012	1,615,403	444,875	638,015
Customer Deposits	2,489,101	2,622,646	2,719,331	2,806,990	2,146,360
Accrued Interest	-	-	720,545	706,934	1,154,286
Liabilities Payable From Restricted Assets:					
Accounts Payable	7,633,220	4,492,364	-	-	-
Accrued Interest	<u>413,442</u>	<u>882,888</u>	<u>166,096</u>	<u>153,270</u>	<u>100,326</u>
Total Current Liabilities	<u>\$ 26,715,313</u>	<u>\$ 24,315,574</u>	<u>\$ 23,863,337</u>	<u>\$ 20,748,525</u>	<u>\$ 24,778,494</u>
Non-Current Liabilities:					
Long-term Debt:					
General Obligation Bonds	\$ 8,396,755	\$ 8,045,029	\$ 7,678,302	\$ 7,291,575	\$ 6,763,127
Certificates of Participation	24,119,352	65,051,790	63,192,774	61,468,693	59,694,612
Revenue Bonds	-	-	-	-	51,255,224
Notes Payable	1,350,778	1,031,730	701,516	359,744	6,010
Other Non-current Liabilities	<u>733,915</u>	<u>890,473</u>	<u>690,709</u>	<u>684,309</u>	<u>684,309</u>
Total Noncurrent Liabilities	<u>\$ 34,600,800</u>	<u>\$ 75,019,022</u>	<u>\$ 72,263,301</u>	<u>\$ 69,804,321</u>	<u>\$118,403,282</u>
Total Liabilities	<u>\$ 61,316,113</u>	<u>\$ 99,334,596</u>	<u>\$ 96,126,638</u>	<u>\$ 90,552,846</u>	<u>\$143,181,776</u>
<b>NET ASSETS</b>					
Invested in Capital Assets, Net of Related Debt	\$361,590,845	\$374,667,591	\$372,696,591	\$382,410,491	\$377,855,787
Restricted for Net OPEB Asset	-	2,071,307	5,649,008	6,204,876	-
Restricted for Debt Service	-	-	3,762,106	1,797,512	5,192,111
Unrestricted	<u>60,474,482</u>	<u>70,282,627</u>	<u>74,719,712</u>	<u>69,931,992</u>	<u>80,204,428</u>
Total Net Assets	<u>\$422,065,327</u>	<u>\$447,021,525</u>	<u>\$456,827,417</u>	<u>\$460,344,871</u>	<u>\$463,252,326</u>

Source: Otay Water District Audited Financial Statements.

## Historical Debt Service Coverage

Table No. 9 below sets forth historical Taxes and Net Revenues and Debt Service Coverage for the last five Fiscal Years.

**TABLE NO. 9**  
**HISTORICAL TAXES AND NET REVENUES (in '000's) AND DEBT SERVICE COVERAGE**  
**For the Fiscal Year ended June 30**

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
Number of New Connections	884	639	171	141	255
Revenues:					
Water Sales	\$43,756	\$48,606	\$50,809	\$52,399	\$56,210
Connection Fees	1,358	1,540	1,481	1,522	1,908
Other Income	784	874	1,855	1,938	181
Availability Fees <sup>(1)</sup>	558	706	688	575	619
Annexation Fees	1,257	2,120	526	392	556
Capacity Fees	6,715	8,028	1,962	1,851	1,948
Investment Earnings	<u>3,174</u>	<u>4,349</u>	<u>3,947</u>	<u>2,157</u>	<u>1,324</u>
Total Revenue	\$57,602	\$66,223	\$61,268	\$60,834	\$62,746
Operation and Maintenance Costs:					
Water Purchases <sup>(2)</sup>	\$25,460	\$27,494	\$28,187	\$29,310	\$31,818
Utilities	2,114	2,419	2,550	2,842	2,223
Payroll	12,885	13,980	16,488	16,391	16,157
Administrative	4,797	6,156	6,815	6,866	5,181
Materials and Maintenance	<u>2,264</u>	<u>2,365</u>	<u>2,381</u>	<u>1,792</u>	<u>1,706</u>
Total Operation and Maintenance Costs	<u>\$47,520</u>	<u>\$52,413</u>	<u>\$56,421</u>	<u>\$57,201</u>	<u>\$57,085</u>
Net Revenues	\$10,082	\$13,810	\$ 4,847	\$ 3,633	\$ 5,661
Taxes <sup>(3)</sup>	<u>\$ 1,338</u>	<u>\$ 2,930</u>	<u>\$ 3,280</u>	<u>\$ 3,430</u>	<u>\$ 3,009</u>
Taxes and Net Revenues	\$11,420	\$16,740	\$ 8,127	\$ 7,063	\$8,669
Debt Service:					
1996 Installment Payments	\$ 760	\$ 757	\$ 651	\$ 542	\$ 580
2004 Installment Payments	948	923	929	928	929
2007 Installment Payments	-	558	1,721	2,491	2,493
2010 Installment Payments	-	-	-	-	518
Letter of Credit Fees	<u>67</u>	<u>66</u>	<u>67</u>	<u>63</u>	<u>129</u>
Total Debt Service	\$ 1,775	\$ 2,304	\$ 3,368	\$ 4,024	\$ 4,649
Coverage Ratio	643%	727%	241%	176%	186%

Source: Otay Water District.

<sup>(1)</sup> Includes only water availability charges not exceeding \$10 per acre per year. To the extent such fees over \$10 per acre are authorized for operational purposes, they are included in "Other Income."

<sup>(2)</sup> This District is disputing approximately \$700,000 of water purchase costs charged by the City of San Diego for potable water between July 2006 and January 2008, which have been excluded from the amounts shown above.

<sup>(3)</sup> ERAF Shift reflected in Taxes for Fiscal Year 2005/06. See "THE WATER SYSTEM - Taxes."

## Projected Debt Service Coverage

The projections of Revenues and the corresponding Taxes and Net Revenues shown in Table No. 10 are based on the assumptions shown below. The District believes the assumptions upon which the projections are based are reasonable; however, some assumptions may not materialize and unanticipated events and circumstances may occur (see "RISK FACTORS"). To the extent that the assumptions are not actually realized, the District's ability to timely make the Installment Payments may be adversely affected.

Following is a discussion of assumptions used in the projection of Revenues, Net Revenues and Taxes:

- (a) The District hired MarketPointe Realty Advisors, San Diego, California, to project development of residential and commercial units within the District over the next six years. Based on that forecast, potable connections in equivalent dwelling units are projected to increase as follows for an overall 6.3% increase during the next six year period and recycled connections are also projected to increase 6.7% during the next six year period as follows.

	Potable System		Recycled System	
	Number of Meters (EDU)	% Increase	Number of Meters (EDU)	% Increase
2012	420	0.6%	20	0.5%
2013	605	0.9%	44	1.1%
2014	629	0.9%	47	1.1%
2015	841	1.2%	41	1.0%
2016	896	1.3%	54	1.3%

- (b) Water sales volume (in acre feet) is projected as follows. The District is projecting a 3.1% decrease in potable water sales from originally budgeted amounts for 2010/11 due to conservation efforts, economic conditions and above average rainfall and a 7.7% decrease in recycled water sales from originally budgeted amounts for 2010/11. The District is also projecting some future increases as rainfall returns to normal.

	Potable System	Recycled System	Total
2011	28,267	3,816	32,083
2012	28,946	3,960	32,906
2013	29,452	4,041	33,493
2014	29,976	4,126	34,102
2015	30,333	4,156	34,489
2016	30,712	4,196	34,908

The District receives a credit of \$185 per acre foot and \$200 per acre foot from MWD and SDCWA, respectively, for each acre foot of recycled water. These credits are included in Water Sales revenue.

- (c) Water rates increased 10.9% on January 1, 2011 and are projected to increase 7.7% on January 1, 2012. For the years 2013 and 2014 they are projected to increase by 7.7% annually and in 2015, a 4.9% water rate increase is projected (see "Water Charges – Proposition 218" herein).
- (d) Capacity and annexation fee rates are estimated to increase 3% in each year from existing rates based on the projected Engineering News-Record index increases. Revenue from these fees will also increase as the number of connections increase as shown in (a) above.

- (e) Water availability charges included in Availability Fees are limited to an amount not exceeding \$10 per acre per year. To the extent the water availability charges exceeding \$10 per acre are authorized for operational purposes, such fees are included in Other Income.
- (f) Taxes do not include *ad valorem* taxes levied for the purpose of paying debt service on the District's 1998 General Obligation Refunding Bonds. Taxes are projected to increase slightly for 2011/12 by \$133,000 based on an increase in assessed value, and slowly increase by approximately 2%, annually. No additional ERAF deductions or Proposition 1A borrowings are assumed (see "Taxes" herein).
- (g) Non-operating income is excluded from the projection. Non-operating revenues within "Miscellaneous Revenues" shown in the District's financial statements consist of property rental and golf course income.
- (h) Water Supply costs are anticipated to increase annually as a result of increases in cost of purchased water, effects of changes in weather, and usage by new customers as follows:

2012	8.6%
2013	9.1%
2014	9.6%
2015	8.0%
2016	7.8%

- (i) Operating costs shown in Fiscal Year 2010/11 are based on current year estimates. Costs for subsequent Fiscal Years are based on the 2011/12 estimates with the annual inflationary factors shown below.

Utilities	3.5%
Materials and Maintenance	4.0%
Administrative Costs	3.0%
Salaries	5.1%
Medical Benefits	9.5%
Workers Comp	5.0%
Other Benefits	3.0%

Base operating costs are also increased based on the projected growth in District operations, similar to the growth rates shown for connections in (a) above.

- (j) The debt service on the 1996 Certificates is calculated based on the existing principal repayment schedule and the Bond Buyer 25 Year Revenue Bond Index as of January 27, 2010 of 4.99%. The current letter of credit expires in June 2011. Further annual letter of credit fees are estimated beginning at 85 basis points of the outstanding par amount of the 1996 Certificates, declining to 50 basis points by 2012/13.

**TABLE NO. 10**  
**PROJECTED TAXES AND NET REVENUES (in '000's) AND DEBT SERVICE COVERAGE**  
**For the Fiscal Year ended June 30**

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Revenues:						
Water Sales	\$ 58,200	\$ 65,304	\$ 71,350	\$ 77,988	\$ 84,162	\$ 89,305
Connection and Other Fees	1,947	1,718	1,813	1,851	1,911	1,954
Availability Fees	601	646	653	660	669	678
Annexation Fees	-	-	-	21	104	196
Capacity Fees	2,589	3,518	5,242	5,489	7,882	8,798
Betterment Fees	677	629	632	638	644	651
Investment Earnings	728	782	993	1,266	1,579	2,167
BABS Subsidy <sup>(1)</sup>	<u>717</u>	<u>830</u>	<u>830</u>	<u>830</u>	<u>830</u>	<u>830</u>
Total Revenue	\$ 65,459	\$ 73,426	\$ 81,513	\$ 88,743	\$ 97,780	\$104,579
Operation and Maintenance Costs:						
Water Purchases	\$ 33,397	\$ 38,244	\$ 41,761	\$ 45,741	\$ 49,402	\$ 53,232
Utilities	2,248	2,359	2,488	2,463	2,578	2,702
Payroll	16,405	17,210	17,788	18,224	18,537	18,807
Administrative	4,185	4,127	4,352	4,469	4,616	4,771
Materials and Maintenance	<u>1,936</u>	<u>2,544</u>	<u>2,653</u>	<u>3,016</u>	<u>3,146</u>	<u>3,282</u>
Total Operation and Maintenance Costs	\$ 58,171	\$ 64,484	\$ 69,042	\$ 73,912	\$ 78,280	\$ 82,793
Net Revenues	\$ 7,288	\$ 8,942	\$ 12,471	\$ 14,831	\$ 19,500	\$ 21,786
Taxes	<u>\$ 3,145</u>	<u>\$ 3,142</u>	<u>\$ 3,142</u>	<u>\$ 3,205</u>	<u>\$ 3,269</u>	<u>\$ 3,433</u>
Taxes and Net Revenues	\$ 10,433	\$ 12,084	\$ 15,613	\$ 18,036	\$ 22,768	\$ 25,220
Debt Service:						
1996 Installment Payments <sup>(2)</sup>	\$ 565	\$ 1,020	\$ 1,134	\$ 1,169	\$ 1,142	\$ 1,209
2004 Installment Payments	928	927	923	922	924	924
2007 Installment Payments	2,497	2,497	2,498	2,497	2,500	2,501
2010 Installment Payments <sup>(1)</sup>	2,548	3,707	3,693	3,675	3,665	3,654
Proposed Debt	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>802</u>	<u>1,022</u>
Total Debt Service	\$ 6,538	\$ 8,151	\$ 8,248	\$ 8,263	\$ 9,033	\$ 9,310
Coverage Ratio <sup>(2)</sup>	160%	148%	189%	218%	252%	271%

Source: Otay Water District.

<sup>(1)</sup> For the purpose of calculating the coverage ratio, when the 1996 Certificates, 2004 Certificates and 2007 Certificates are no longer outstanding, the Interest Subsidy Payments will be deducted from Net Revenues and the calculation of Debt Service payable by the District on Parity Bonds or Contracts will be reduced by the amount of the Interest Subsidy Payments the District is entitled to receive during such twelve-month period.

<sup>(2)</sup> Based on April 14, 2011 25-Year Revenue Bond Index of 5.58% plus letter of credit fees.

The projected Revenues, Taxes and Operation and Maintenance Costs shown above are subject to several variables as described on the previous pages. The District provides no assurance that the projected Taxes and Net Revenues will be achieved (see "RISK FACTORS" herein).

## **RISK FACTORS**

*The following information should be considered by prospective investors in evaluating the 1996 Certificates. However, the following does not purport to be an exhaustive listing of risks and other considerations which may be relevant to investing in the 1996 Certificates. In addition, the order in which the following information is presented is not intended to reflect the relative importance of any such risks.*

### **System Demand**

There can be no assurance that the local demand for service provided by the Water System will increase to levels described in this Official Statement under the heading "THE WATER SYSTEM." Reduction in the level of new connections could require an increase in rates or charges in order to produce Taxes and Net Revenues sufficient to comply with the District's rate covenant in the Installment Purchase Agreement. Such rate increases could increase the likelihood of nonpayment, and could also further decrease demand. Furthermore, there can be no assurance that any other entity with regulatory authority over the Water System will not adopt further restrictions on operation of the Water System.

### **Increased Operation and Maintenance Costs**

There can be no assurance that operation and maintenance costs of the Water System will be consistent with the levels contemplated in this Official Statement. Changes in technology, increases in the cost of operation, increased water treatment requirements or other costs mandated by regulatory agencies or other expenses could require increases in rates or charges in order to comply with the rate covenant described herein and in the Installment Sale Agreement, and could increase the possibility of nonpayment of the 1996 Certificates.

### **Additional Obligations Payable from Taxes and Net Revenues**

The District may issue additional parity obligations or enter into additional Contracts payable from Taxes and Net Revenues on a parity with its pledge of such Taxes and Net Revenues to the Installment Payments relating to the 1996 Certificates and the Existing Parity Obligations. The ability of the District to enter into such Parity Debt is subject to certain requirements set forth in the 1996 Installment Sale Agreement, the 2004 Installment Purchase Agreement, the 2007 Installment Purchase Agreement and the 2010 Installment Purchase Agreement. See "SOURCES OF PAYMENT FOR THE CERTIFICATES - Parity Debt."

The District may also enter into obligations payable from Taxes and Net Revenues which are subordinate to the 1996 Certificates.

### **Risks Relating to Water Supplies**

The District's current potable water supply primarily comes from purchases from SDCWA, which in turn currently purchases approximately 87% of its water supply from MWD and IID. This source of water could become limited due to possible events that include prolonged droughts or similar changes in State-wide weather patterns, earthquakes or other natural disasters, contamination by environmental hazards, or acts of terrorism or civil unrest. There can be no assurance that currently available water supplies would be sufficient to meet demand under current conditions in the event of a prolonged drought or other interruption of the District's source of water supply, or that the District would be able to secure alternate sources of water to meet its customer demand. See "THE WATER SYSTEM - Water Supply" herein for a discussions of the water supply in the region and the District's sources of water in particular.

## **Environmental Regulation**

The kind and degree of water treatment effected through the water system is regulated, to a large extent, by the federal government and the State of California. Treatment standards set forth in federal and state law control the operations of the water system and mandate the use of water treatment technology. If the federal government, acting through the Environmental Protection Agency, or the State of California, acting through the Department of Health Services, or additional federal or state agencies, should impose stricter water quality standards upon the Water System, the District's expenses could increase accordingly and rates and charges would have to be increased to offset those expenses. It is not possible to predict the direction federal or state regulation will take with respect to water quality standards, although it is likely that, over time, both will impose more stringent standards with attendant higher costs.

## **Proposition 218**

On November 5, 1996, California voters approved Proposition 218-Voter Approval for Local Government Taxes-Limitation on Fees, Assessments, and Charges-Initiative Constitutional Amendment. Proposition 218 added Articles XIIC and XIID to the California Constitution, imposing certain vote requirements and other limitations on the imposition of new or increased taxes, assessments and property-related fees and charges. See "THE WATER SYSTEM - Water Charges - Proposition 218" for a discussion of specific issues and risks raised by Proposition 218. The District's current projections assume future rate increases which will be subject to the Proposition 218 notice process.

## **Casualty Risk; Earthquakes**

Any natural disaster or other physical calamity, including earthquake, may have the effect of reducing Revenues and Taxes through damage to the Water System and/or adversely affecting the economy of the surrounding area. The Installment Purchase Agreement requires the District to maintain insurance or self-insurance, but only if and to the extent available at a reasonable cost from reputable insurers, and the District is not expressly required to provide earthquake insurance. The District is located in a seismically active region and structures in the District could be impacted by a major earthquake originating from the numerous faults in the area. Seismic hazards encompass both potential surface rupture and ground shaking. In the event of total loss of the Water System, there can be no assurance that insurance proceeds will be adequate to rebuild the Water System or to redeem all Outstanding 1996 Certificates or that losses in excess of the insured amount will not occur.

## **Early Prepayment Risk**

Early prepayment of the 1996 Certificates may occur in whole or in part without premium, on any date, if the District exercises its right to prepay the 1996 Certificates in whole or in part pursuant to the provisions of the Trust Agreement. Mandatory prepayment of the 1996 Certificates may occur upon the expiration, substitution or termination of the Letter of Credit (see "THE CERTIFICATES - Prepayment").

## **Limited Recourse on Default**

If the District defaults on its obligation to pay the Installment Payments when due, the Trustee, subject to certain rights of the Bank, has the right to accelerate the total unpaid principal amount of the Installment Payments. However, in the event of a default and such acceleration there can be no assurance that the District will have sufficient Taxes and Net Revenues to pay the accelerated principal. Default by the District will not result in loss of the 1996 Project or the Water System or any other assets of the District.

So long as the 1996 Certificates are in book-entry form, DTC (or its nominee) will be the sole registered owner of the 1996 Certificates, and the rights and remedies of the Certificate Owners will be exercised through the procedures of DTC.

## **Bankruptcy Risks**

The enforceability of the rights and remedies of the owners of the 1996 Certificates and the obligations of the District may become subject to the following: the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditors' rights generally, now or hereafter in effect; usual equitable principles which may limit the specific enforcement under state law of certain remedies: the exercise by the United States of America of the powers delegated to it by the federal Constitution; and the reasonable and necessary exercise, in certain exceptional situations of the police power inherent in the sovereignty of the State of California and its governmental bodies in the interest of servicing a significant and legitimate public purpose. Bankruptcy proceedings, or the exercise of powers by the federal or state government, if initiated, could subject the owners of the 1996 Certificates to judicial discretion and interpretation of their rights in bankruptcy or otherwise and consequently may entail risks of delay, limitation, or modification of their rights.

## **No Obligation to Tax**

The obligation of the District to pay Installment Payments does not constitute an obligation of the District for which the District is obligated to levy or pledge any form of taxation or for which the District has levied or pledged any form of taxation, except the Taxes. The obligation of the District to pay Installment Payments does not constitute a debt or indebtedness of the District, the State of California or any of its political subdivisions, within the meaning of any constitutional or statutory debt limitation or restriction.

## **Change in Law**

In addition to the other limitations described herein, the California electorate or Legislature could adopt a constitutional or legislative initiative with the effect of reducing revenues payable to or collected by the District. There is no assurance that the California electorate or Legislature will not at some future time approve additional limitations that could have the effect of reducing the Taxes and Net Revenues and adversely affecting the security of the 1996 Certificates.

## **Loss of Tax Exemption**

In order to maintain the exclusion from gross income for federal income tax purposes of the interest on the 1996 Certificates, the District has covenanted in the Installment Sale Agreement to comply with each applicable requirement of Section 103 and Sections 141 through 150 of the Internal Revenue Code. The interest on the 1996 Certificates could become includable in gross income for purposes of federal income taxation retroactive to the date of execution and delivery of the 1996 Certificates, as a result of acts or omissions of the District in violation of this or other covenants in the Installment Sale Agreement or the Trust Agreement. Should such an event of taxability occur, the 1996 Certificates are not subject to prepayment or any increase in interest rates and will remain outstanding until maturity or until prepaid under one of the redemption provisions contained in the Trust Agreement. See "LEGAL MATTERS - Tax Matters" herein.

## **Risks Relating to Build America Bonds Interest Subsidy**

The District must comply with certain requirements of the Code in order for the 2010B Bonds to be treated as qualified bonds and to continue to be eligible for the Interest Subsidy Payment. The District has covenanted to comply with each of these requirements. However, failure by the District to comply with these requirements may result in a delay or forfeiture of all or a portion of the Interest Subsidy Payment and may cause the 2010B Bonds to cease to be treated as qualified bonds either prospectively from the date of determination of a failure to comply with the requirements or retroactively to the date of execution and delivery of the 2010B Bonds. Should such an event occur, the 2010B Bonds are subject to

extraordinary prepayment. If the District is obligated to provide for the issuance of refunding obligations in order to redeem the 2010B Bonds prior to their maturity, the District would be subject to the various risks attendant to issuance of refunding obligations, including higher-than-desired interest rates and duplicative transaction costs. In addition, it is important to note that Build America Bonds are a new product introduced by the American Recovery and Reinvestment Act, which was signed into law on February 17, 2009. The Interest Subsidy Payments do not constitute a full faith and credit guarantee of the United States government, but are required to be paid by the Treasury under the American Recovery and Reinvestment Act. As such, the District can provide no assurance that future legislation or clarifications or amendments to the Code, if enacted into law, or future court decisions will not reduce or eliminate the Interest Subsidy Payment with respect to the 2010B Bonds. The Treasury may offset any Interest Subsidy Payments to which the Otay Water District Financing Authority (the "Authority") is otherwise entitled against any other tax liability of the Authority payable to the Treasury, such as withholding or payroll taxes, or other penalties or interest that may be owed at any time to the Treasury. The District is obligated under the 2010 Installment Purchase Agreement for the 2010 Bonds to make those installment payments without regard to the receipt or deposit of Interest Subsidy Payments. If the Interest Subsidy is delayed or forfeited, it will cause a reduction in Net Revenues available to pay Installment Payments and payments due with respect to the Existing Parity Obligations.

## **LEGAL MATTERS**

### **Enforceability of Remedies**

The remedies available to the Trustee and the Owners of the 1996 Certificates upon an event of default under the Trust Agreement, the Installment Sale Agreement or any other document described herein are in many respects dependent upon regulatory and judicial actions which are often subject to discretion and delay. Under existing law and judicial decisions, the remedies provided for under such documents may not be readily available or may be limited. The various legal opinions to be delivered concurrently with the delivery of the 1996 Certificates will be qualified to the extent that the enforceability of certain legal rights related to the Trust Agreement and Installment Sale Agreement are subject to limitations imposed by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally and by equitable remedies and proceedings generally.

### **Approval of Legal Proceedings**

Certain legal matters related to this Reoffering Memorandum will be passed upon by Best Best & Krieger LLP, as Special Counsel, for the District by its General Counsel and by Stradling Yocca Carlson & Rauth, a Professional Corporation, and for the Bank by its counsel, Musick, Peeler and Garrett, LLP. The Series 1995 Bonds are available for delivery through the DTC book-entry system.

## **Tax Matters**

### **Original Opinion**

On June 18, 1996, Best Best & Krieger LLP, Special Counsel to the District in connection with the execution and delivery of the 1996 Certificates, delivered their opinion to the effect that, based upon an analysis of then existing statutes, regulations, rulings and judicial decisions, and assuming, among other matters, compliance with certain covenants and requirements, the interest component of the Installment Payments made by the District under the Installment Sale Agreement and received by the Certificate Owners was excluded from gross income for federal income tax purposes, was not an item of tax preference for purposes of federal individual or corporate alternative minimum tax, but such interest component may be included in the calculation of corporation alternative minimum taxable income, and such interest component is exempt from State of California personal income taxes. A complete copy of

the opinion of Special Counsel delivered at the original execution and delivery of the 1996 Certificates is set forth in "APPENDIX D" hereto.

### **No Updated Special Counsel Opinion**

Special Counsel has not taken, and does not intend to take, any action to update their original opinions or to determine if the interest component of the Installment Payments is presently excluded from gross income for federal income tax purposes or exempt from State of California personal income taxes.

### **General Considerations**

Notwithstanding the foregoing, investors should be aware of the following information.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the interest component of the Installment Payments relating to the 1996 Certificates. The District has made certain representations and covenanted to comply with certain restrictions, conditions and requirements designed to ensure that the interest component of the Installment Payments relating to the 1996 Certificates will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in the interest component of the Installment Payments relating to the 1996 Certificates being included in gross income for federal income tax purposes, possibly from the date of original issuance of the 1996 Certificates. The opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates assumed the accuracy of these representations and compliance with these covenants. Special Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken), or events occurring (or not occurring), or any other matters coming to Special Counsel's attention after the date of execution and delivery of the 1996 Certificates may adversely affect the value of, or the tax status of interest with respect to, the 1996 Certificates. Accordingly, the opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates is not intended to, and may not, be relied upon in connection with any such actions, events or matters.

Although Special Counsel has rendered an opinion that interest component of the Installment Payments relating to the 1996 Certificates is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of interest with respect to, the 1996 Certificates may otherwise affect a Beneficial Owner's federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial Owner or the Beneficial Owner's other items of income or deduction. Special Counsel express no opinion regarding any such other tax consequences.

Future legislative proposals, if enacted into law, clarification of the Code or court decisions may cause interest component of the Installment Payments relating to the 1996 Certificates to be subject, directly or indirectly, to federal income taxation or to be subject to or exempted from state income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such future legislative proposals, clarification of the Code or court decisions may also affect the market price for, or marketability of, the 1996 Certificates. Prospective purchasers of the remarketed 1996 Certificates should consult their own tax advisors regarding any pending or proposed federal or state tax legislation, regulations or litigation, as to which Special Counsel expresses no opinion.

The opinion of Special Counsel delivered in connection with the initial execution and delivery of the 1996 Certificates was based on current legal authority existing as of June 18, 1996, covered certain matters not directly addressed by such authorities, and represented Special Counsel's judgment as to the proper treatment of the 1996 Certificates for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Special Counsel cannot give and has not given any opinion or assurance about the future activities of the District, or about the effect of future changes in the

Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The District has covenanted, however, to comply with the requirements of the Code.

Special Counsel's engagement with respect to the 1996 Certificates ended on June 18, 1996 with the original execution and delivery of the 1996 Certificates. Unless separately engaged, Special Counsel is not obligated to defend the District or the Beneficial Owners regarding the tax-exempt status of the interest component of the Installment Payments relating to the 1996 Certificates in the event of an audit examination by the IRS. Under current procedures, parties other than the District and their appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax-exempt bonds is difficult, obtaining an independent review of IRS positions with which the District legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the 1996 Certificates for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the 1996 Certificates and may cause the District or the Beneficial Owners to incur significant expense.

## **Litigation**

There is no action, suit or proceeding known to be pending or threatened, restraining or enjoining the District in the execution or delivery of, or in any way contesting or affecting the validity of, the 1996 Certificates. There is no litigation known to be pending, or to the knowledge of the District, threatened, questioning the existence of the District or the title of the officers of the District to their respective offices.

There exist lawsuits and claims against the District, which are incidental to the ordinary course of operations of the District's water system and related activities. In the view of the District's management and of the General Counsel to the District, there is no litigation, present or pending, which will individually or in the aggregate materially impair the District's ability to service its indebtedness or which will have a material adverse effect on the business operations of the District.

## **CONCLUDING INFORMATION**

### **Rating on the Certificates**

In connection with this Reoffering Memorandum, it is expected that Standard & Poor's Ratings Services ("S&P") will assign the 1996 Certificates the rating of "A-1/A+", with the understanding that the Letter of Credit will be issued by the Bank on June 30, 2011. The rating should be evaluated independently of any other rating of the District. No application has been made to any other rating agency in order to obtain additional ratings on the 1996 Certificates. The credit enhanced rating on the 1996 Certificates reflect the S&P's current assessment of the creditworthiness of the Bank and its ability to pay draws under the Letter of Credit. Any further explanation as to the significance of the above rating may be obtained from S&P.

The above described rating is not recommendations to buy, sell or hold the 1996 Certificates, and such rating may be subject to revision or withdrawal at any time by S&P. Neither the District nor the Remarketing Agent undertake any responsibility either to bring to the attention of the owners of the 1996 Certificates the downward revision or withdrawal of any rating obtained or to oppose any such revision or withdrawal. Any downward revision or withdrawal of the rating may have an adverse effect on the market price of the 1996 Certificates.

## **Remarketing Agent**

J.P. Morgan Securities LLC serves as Remarketing Agent for the 1996 Certificates. The Remarketing Agent will carry out the duties and obligations provided for the Remarketing Agent under and in accordance with the provisions of the Trust Agreement and the Remarketing Agreement, by and between the District and the Remarketing Agent, dated as of June 1, 1996. The principal office of the Remarketing Agent (for purposes of its responsibilities as Remarketing Agent) is New York, New York.

## **Additional Information**

The summaries and references contained herein with respect to the Trust Agreement, the Installment Sale Agreement, the 1996 Certificates, statutes and other documents, do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute and references to the 1996 Certificates are qualified in their entirety by reference to the form thereof included in the Trust Agreement. Definitions of certain terms used herein are set forth in "APPENDIX A." Copies of the Trust Agreement and the Installment Sale Agreement are available for inspection from the District, 2554 Sweetwater Springs Blvd., Spring Valley, California 91978.

## **References**

Any statements in this Reoffering Memorandum involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Reoffering Memorandum is not to be construed as a contract or agreement between the District and the purchasers or Owners of any of the 1996 Certificates.

## **Execution**

The execution of this Reoffering Memorandum has been duly authorized by the Otay Water District.

### **OTAY WATER DISTRICT**

By: \_\_\_\_\_

**General Manager**

## APPENDIX A

### SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The following is a summary of certain provisions of the Installment Sale Agreement and the Trust Agreement which are not described elsewhere in the Official Statement. These summaries do not purport to be comprehensive and reference should be made to the Installment Sale Agreement and the Trust Agreement for a full and complete statement of their respective provisions. All capitalized terms used and not defined in the Official Statement have the meanings set forth in the Installment Sale Agreement or the Trust Agreement.

Unless the context otherwise requires, the terms defined under this caption will for all purposes of the Official Statement have the meanings herein specified.

“Accountant’s Report” means a report signed by an Independent Certified Public Accountant.

“Additional Costs” shall mean those costs the District is required to pay as more particularly set forth in the Installment Sale Agreement.

“Agreement” or “Installment Sale Agreement” means the Installment Sale Agreement as originally executed or as it may be from time to time amended as provided for therein, including as amended by the First Supplement to Installment Sale Agreement.

“Authorized Denomination” means (i) while the Certificates bear interest at a Daily, Weekly, Monthly or CP Rate, \$100,000, and (ii) while the Certificates bear interest at a Tender or Fixed Rate, \$5,000, and in all cases, whole multiples thereof; provided that one or more Certificates may be in a denomination less than \$100,000 while the Certificates bear interest of a Daily, Weekly, Monthly or CP rate in order to match sinking fund installments set forth in the Trust Agreement.

“Bank” means Union Bank, N.A., as issuer of the Facility, until a Substitute Facility is issued and effective in accordance with the Trust Agreement, and thereafter “Bank” shall mean the obligor on such Substitute Facility. If the Facility is provided by more than one financial institution or insurance company as permitted by the Trust Agreement the term “Bank” shall be modified as necessary as permitted by the Trust Agreement.

“Bank Certificates” means Certificates purchased with amounts drawn on the Facility pursuant to the Trust Agreement and owned by and registered to the Bank or its nominee or transferee.

“Bank Rate” means the rate or rates per annum payable with respect to each Bank Certificate, which shall be as provided in the Reimbursement Agreement dated as of June 30, 2011 by and between the Bank, the Corporation and the District relating to the Letter of Credit, or, in the event that a Substitute Facility is in effect, as may be provided in such other agreement relating to such Substitute Facility as may be applicable thereto, provided that such rate shall not exceed the maximum rate permitted by applicable law.

“Business Day” means any day of the year other than Saturday or Sunday on which banks in New York, New York, and in Los Angeles, California and any other city in which the principal office of the Bank may be located are not authorized or required by law or executive order to close and on which the New York Stock Exchange is not closed.

“Certificate Payment Fund” means the fund by that name established in the Trust Agreement.

“Certificate Year” means the period beginning on the date of execution and delivery of the Certificates and ending on September 1, 1996, and each successive one-year or shorter period thereafter beginning on September 2 and ending on September 1 until there are no Outstanding Certificates.

“Code” means the Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder.

“Debt Service Account” means the account by that name established pursuant to the Trust Agreement.

“Default Rate” shall have the meaning as set forth in the Reimbursement Agreement.

“District Payments Account” means the accounts by that name established pursuant to the Trust Agreement.

“Eligible Funds” means:

(a) Certificate proceeds deposited with the Trustee contemporaneously with the delivery and sale of the Certificates (other than proceeds of sale of Certificates to the District) and which were continuously thereafter subject to the lien of the Trust Agreement in a separate and segregated fund, account or subaccount established hereunder in which no moneys which were not Eligible Funds were at any time held, together with the investment earnings thereon;

(b) Moneys (i) held in any fund, account or subaccount established hereunder in which no, other moneys which are not Eligible Funds are held, and (ii) which have been on deposit with the Trustee for at least three hundred sixty-seven (367) consecutive days during which period no Event of Bankruptcy shall have occurred, together with the investment earnings thereon;

(c) Proceeds of a drawing under the Facility and interest earned on such proceeds; and

(d) Proceeds from the issuance and sale of refunding bonds or other evidence of indebtedness and interest earned on such proceeds and any other moneys deposited with the Trustee if there is delivered to the Trustee at the time of the issuance and sale of such refunding bonds or other evidence of indebtedness or the deposit of such other moneys with the Trustee a written opinion of counsel acceptable to the Rating Agency experienced in bankruptcy matters to the effect that payments with such proceeds or other moneys, as the case may be, of principal of, premium, if any, or interest on the Bonds would not be avoidable as avoidable transfers under the United States Bankruptcy Code should an Event of Bankruptcy hereafter occur.

“Event of Bankruptcy” means the filing of a petition in bankruptcy or the commencement of a proceeding under the United States Bankruptcy Code pursuant to Sections 301 or 303 thereof by or against the District.

“Event of Default” means an event of default under the Installment Sale Agreement, and an event of default under the Trust Agreement.

“Facility” means the Letter of Credit and any Substitute Facility.

“Federal Securities” means any of the following which are noncallable and which at the time of investment are legal investments under the laws of the State of California, as shall be certified in writing by the District to the Trustee, for the moneys proposed to be invested therein:

(a) direct general obligations of (including obligations issued or held in book entry form on the books of the Department of the Treasury of the United States of America), or obligations the payment of principal of and interest on which are directly or indirectly unconditionally guaranteed by, the United States of America; and

(b) direct obligations of any department, agency or instrumentality of the United States of America the timely payment of principal of and interest on which are fully guaranteed by the United States of America.

“First Supplement to Installment Sale Agreement” means the First Supplement to Installment Sale Agreement by and between the Corporation, the District and the Trustee, dated as of June 1, 2011.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the last day of June of the following calendar year, or any other twelve-month period selected and designated as the official Fiscal Year of the District.

“Fixed Rate Conversion Date” means a Conversion Date with respect to a Fixed Rate.

“Gross Revenues” means (i) all water availability charges imposed pursuant to Chapter 2 of Part 5 of the Law not exceeding \$10 per acre per year; (ii) all income, rents, rates, fees, charges and other moneys derived by the District from the ownership or operation of the Water System, including, without limiting the generality of the foregoing, (a) all income, rents, rates, fees, charges or other moneys derived from the sale, furnishing, and supplying of water and other services, facilities and commodities sold, furnished or supplied through the facilities of the Water System, including connection fees, (b) the earnings on and income derived from the investment of such income, rents, rates, fees and charges or other moneys, and (c) the proceeds derived by the District directly or indirectly from the sale, lease or other disposition of a part of the Water System as permitted hereunder: provided that the term “Gross Revenues” shall not include customers’ deposits or any other deposits subject to refund until such deposits have become the property of the District.

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants appointed by the District, who has a favorable reputation in the field in which its opinion or certified will be given, and:

- (a) is in fact independent and not under domination of the District;
- (b) does not have any substantial interest, direct or indirect, with the District; and
- (c) is not connected with the District as an officer or employee of the District, but who may be regularly retained to make reports to the District.

“Independent Financial Consultant” means a firm of certified public accountants or a consulting engineering firm or engineer, of favorable national or regional reputation, which is not an employee of, or otherwise controlled by, the Corporation, the Trustee or the District.

“Information Services” means the Electronic Municipal Market Access website of the Municipal Securities Rulemaking Board.

“Installment Payment Date” means (1) each date upon which principal component payments are due and payable as set forth on in the Installment Sale Agreement, and (2) each Interest Payment Date.

“Installment Payment Fund” means that fund by that name established pursuant to the Installment Sale Agreement.

“Installments” or “Installment Payments” means the installment payments payable by District pursuant to the Installment Sale Agreement during the Term.

“Interest Payment Date” means:

(a) When the Certificates represent interest at the Daily, Weekly or Monthly Rate, the first Business Day of each calendar month except with respect to the first Interest Payment Date after the Delivery Date which shall be August 1, 2011;

(b) When the Certificates represent interest at a CP Rate, the first Business day immediately following the last day of each CP Rate Period applicable thereto;

(c) When the Certificates represent interest at the Fixed Rate, the first day of each March and September; and

(d) For the Certificates which are subject to mandatory tender pursuant to the Trust Agreement, the date of the mandatory tender (regardless of whether a Holder elects to retain any such Certificates on such date).

“Management Consultant” means any Person of national reputation qualified to report on questions relating to the financial condition of health care facilities, selected by the District, and who (i) is in fact independent of and not under the control of the District, (ii) does not have any substantial interest direct or indirect in the District, and (iii) is not connected with the District as a director, officer or employee of the District, but who may be regularly retained by the District to make annual or other regular reports to the District.

“Maximum Interest Rate” means the lesser of 12% or the maximum amount permitted by State of California law.

“Minimum Permitted Investment Rating” means a rating of “Aa” or better by Moody’s Investors Service or “AA” or better by Standard & Poor’s Ratings Group or “AA” or better by Fitch Investors Service, Inc. or “A” or better by A.M. Best and Company, determined without regard to whether such rating is qualified by a conditional or provisional modifier.

“Moody’s” means Moody’s Investors Service, 99 Church Street, New York, New York 10007, a corporation organized and existing under the laws of the State of Delaware, except that if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, then the term “Moody’s” shall be deemed to refer to any other nationally recognized securities rating agency selected by the District upon written notice to the Trustee and the Bank.

“Net Proceeds” means any insurance or condemnation award paid with respect to the Project, or any proceeds resulting from the sale of any or all portions of the Project remaining after payment therefrom of all expenses incurred in the collection thereof.

“Net Revenues” means Gross Revenues less Operation and Maintenance Expenses.

“Operation and Maintenance Expenses” means all expenses and costs of management, operation, maintenance and repair of the Water System, and all incidental costs, fees and expenses properly chargeable to the Water System and any rebate to the United States Government pursuant to the Code (but excluding debt service or other similar payments on Parity Debt or other obligations and depreciation and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature), all as determined in accordance with generally accepted accounting practices.

“Opinion of Bond Counsel” means a written opinion of nationally recognized bond counsel (who may be counsel for the District) acceptable to the District and the Trustee to the effect that the action proposed to be taken is authorized or permitted by the laws of the State, the Trust Agreement and the Installment Sale Agreement and will not adversely affect the validity of the Installment Sale Agreement or the Certificates under the laws of the State or the exclusion from gross income for federal income tax purposes of interest with respect to the Certificates.

“Outstanding,” when used as of any particular time with reference to Certificates or Parity Debt, means all Certificates and Parity Debt except --

(1) Certificates (or portions of Certificates) or Parity Debt canceled by the Trustee or delivered to the Trustee for cancellation;

(2) Certificates (or portions of Certificates) or Parity Debt (or portions of Parity Debt) paid or deemed to have been paid within the meaning defined in the Trust Agreement;

(3) Certificates or Parity Debt in lieu of or in substitution for which other Certificates or Parity Debt shall have been executed and delivered by the Trustee pursuant to the Trust Agreement; and

(4) Untendered Certificates.

“Owner” or “Holder” or “Certificate Owner” or “Certificate Holder” or “Owner of Certificates” or “Holder of Certificates” or any similar term, when used with respect to the Certificates, means any person who shall be the registered owner of any Outstanding Certificate. “Owner” or “Holder” or “Certificate Owner” or “Certificate Holder” or “Owner of Certificates” or “Holder of Certificates” shall mean the Bank or the nominee of the Bank with respect to any Bank Certificates.

“Parity Debt” means the 2004 Certificates, the 2007 Certificates and the 2010 Bonds and indebtedness or other obligations (including leases and installment sale agreements) issued or incurred by the District and secured by a pledge of and lien on Taxes and/or Net Revenues equally and ratably with the Installment Payments.

“Permitted Investments” means any of the following which at the time of investment are legal investments under the laws of the State of California for the moneys proposed to be invested therein:

(1) Federal Securities;

(2) direct obligations of the United States of America and securities fully and unconditionally guaranteed as to the timely payment of principal and interest by the United States of America; provided, that the full faith and credit of the United States of America must be pledged to any such direct obligation or guarantee (“Direct Obligations”);

(3) direct obligations and fully guaranteed certificates of beneficial interest of the Export-Import Bank of the United States; consolidated debt obligations and letter of credit-backed issues of the Federal Home Loan Banks; participation certificates and senior debt obligations of the Federal Home Loan Mortgage Corporation (“FHLMCs”); debentures of the Federal Housing Administration; mortgage-backed securities (except stripped mortgage securities which are valued greater than par on the portion of unpaid principal) and senior debt obligations of the Federal National Mortgage Association (“FNMA”); participation certificates of the General Services Administration; guaranteed mortgage-backed securities and guaranteed participation certificates of the Government National Mortgage Association (“GNMA”); guaranteed participation certificates and guaranteed pool certificates of the Small Business Administration; debt obligations and letter of credit-backed issues of the Student Loan Marketing Association; local authority

bonds of the U.S. Department of Housing & Urban Development; guaranteed Title XI financings of the U.S. Maritime Administration; guaranteed transit bonds of the Washington Metropolitan Area Transit Authority; Resolution Funding Corporation securities;

- (4) direct obligations of any state of the United States of America or any subdivision or agency thereof whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "A" or better by Moody's and "A" or better by S&P or any obligation fully and unconditionally guaranteed by any state, subdivision or agency whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "A" or better by Moody's and "A" or better by S&P;
- (5) commercial paper (having original maturities of not more than 270 days) rated, at the time of purchase, "P-1" by Moody's and "A-1" or better by S&P;
- (6) federal funds, unsecured certificates of deposit, time deposits or bankers acceptances (in each case having maturities of not more than 365 days) of any domestic bank including a branch office of a foreign bank which branch office is located in the United States, provided legal opinions are received to the effect that full and timely payment of such deposit or similar obligation is enforceable against the principal office or any branch of such bank, which, at the time of purchase, has a short-term "Bank Deposit" rating of "P-1" by Moody's and a "Short-Term CD" rating of "A-1" or better by S&P;
- (7) deposits of any bank or savings and loan association which has combined capital, surplus and undivided profits of not less than \$3,000,000, provided such deposits are continuously and fully insured by the Bank Insurance Fund or the Savings Association Insurance Fund of the Federal Deposit Insurance Corporation, including deposits of the Trustee or any of its affiliates;
- (8) investments in money-market funds rated "AAAm" or "AAAm-G" by S&P and at least "AA" by Moody's including any such funds advised by or of the Trustee or an affiliate;
- (9) repurchase agreements collateralized by Direct Obligations, GNMA's, FNMA's or FHLMC's with any registered broker/dealer subject to the Securities Investors' Protection Corporation jurisdiction or any commercial bank insured by the FDIC, if such broker/dealer or bank has an uninsured, unsecured and unguaranteed obligation rated "P-1" or "A3" or better by Moody's and "A-1" or "A-" or better by S&P, provided:
  - (a) a master repurchase agreement or specific written repurchase agreement governs the transaction; and
  - (b) the securities are held free and clear of any lien by the Trustee or an independent third party acting solely as agent for the Trustee. and such third party is (i) a Federal Reserve Bank, (ii) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$50,000,000, or (iii) a bank approved in writing for such purpose by the Bank and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee; and
  - (c) a perfected first security interest under the Uniform Commercial Code, or book-entry procedures prescribed at 31 C.F.R. 306.1 *et seq.* or 31 C.F.R. 350.0 *et seq.* in such securities is created for the benefit of the Trustee; and

- (d) the repurchase agreement has a term of 180 days or less, and the Trustee or the Agent will value the collateral securities no less frequently than weekly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within two Business Days of such valuation; and
- (e) the fair market value of the securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 103%;
- (10) the Local Agency Investment Fund maintained by the Treasurer of the State of California;
- (11) any investment agreement or similar investment arrangement with a financial institution, the long-term unsecured obligations of which are rated "AA" or better by Moody's and S&P, by the terms of which the Trustee is required to withdraw all amounts invested therein if such rating falls below "AA"; and
- (12) pre-refunded municipal obligations defined as follows: Any bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on the date specified in the notice; and (A) which are rated, based on the escrow, in the highest rating category of S&P and Moody's or any successors thereto; or (B)(i) which are fully secured as to principal and interest and prepayment premium, if any, by a fund consisting only of cash or noncallable Federal Securities, which fund may be applied only to the payment of such principal of and interest and prepayment premium, if any, on such bonds or other obligations on the maturity date or dates thereof or the specified prepayment date or dates pursuant to such irrevocable instructions, as appropriate, and (ii) which fund is sufficient, as verified by an Independent Certified Public Accountant, to pay principal of and interest and prepayment premium, if any, on the bonds or other obligations described in this paragraph on the maturity date or dates thereof or on the prepayment date or dates specified in the irrevocable instructions referred to above, as appropriate.

"Prepayment Account" means the account by that name established in the Trust Agreement.

"Prepayment Price" means, with respect to any Certificate (or portion thereof), the principal amount with respect to such Certificate (or portion thereof) plus the applicable premium, if any, payable upon prepayment thereof pursuant to the provisions of such Certificate and the Trust Agreement.

"Priority Debt" means indebtedness or other obligations (including other leases and installment sale agreements) issued and incurred by the District and secured by a pledge of and lien on Taxes and/or Net Revenues which is senior to and has priority over the pledge of and lien on Taxes and/or Net Revenues securing payment of the Installment Payments.

"Project" means the public improvements acquired and constructed or to be acquired and constructed by the District with the proceeds of the Certificates, each as more particularly described in the Installment Sale Agreement, or any property substituted therefor in conformance with the Installment Sale Agreement.

"Purchase Date" means the date upon which the Tender Agent is obligated to purchase a Certificate or Certificates pursuant to the Trust Agreement.

"Purchase Price" of any Certificate required to be purchased by the Tender Agent pursuant to the Trust Agreement means an amount equal to the principal amount of such Certificate plus, if the Purchase Date is other than an Interest Payment Date, accrued interest thereon, at the rate applicable to the Certificates from the most recent Interest Payment Date and up to but excluding the Purchase Date.

“Project Purchase Price” means the amount determined pursuant to the Installment Sale Agreement.

“Rating Agencies” means Moody’s and S&P.

“Rebate Fund” means the fund by that name established in the Trust Agreement.

“Record Date” means for the interest payable on any Interest Payment Date means (i) the Business Day immediately prior to the Interest Payment Date in question in the case of the Daily and Weekly Rate Periods, (ii) the last Business Day at least five (5) days prior to the Interest Payment Date in question in the case of the Monthly or CP Rate Periods, and (iii) the 15<sup>th</sup> day (whether or not a Business Day) of the calendar month immediately preceding such Interest Payment Date in the case of a Fixed Rate Period.

“Registrar” means the Trustee or such other entity as the Trustee or the District may designate to act as registrar for the Certificates pursuant to the Trust Agreement.

“Related Documents” means the Trust Agreement, the Facility, the Installment Sale Agreement, the Certificates, the Remarketing Agreement, the Official Statement, the Reoffering Memorandum and any other document or instrument required or stated to be delivered hereunder or thereunder on the Delivery Date.

“Remarketing Agent” means J.P. Morgan Securities LLC, in its capacity as successor remarketing agent for the Certificates, or any successor entity appointed by the District and approved by the Bank to perform the duties of the Remarketing Agent hereunder.

“Remarketing Agreement” means the Remarketing Agreement dated as of June 1, 1996, by and between the District and the Remarketing Agent as amended.

“Reserve Credit Facility” means a policy of insurance, a surety bond, a letter of credit or other comparable credit facility, or a combination thereof, which, together with money on deposit in the reserve fund, if any, provide an aggregate amount equal to the Reserve Requirement, so long as the provider of any such policy of insurance, surety bond, letter of credit or other comparable credit facility is rated in the highest rating category by Standard & Poor’s Ratings Group, Moody’s Investors Service or A.M. Best & Company.

“Responsible Officer” means any officer of the Trustee assigned to administer its duties under the Trust Agreement.

“Revenue Fund” means the fund by that name established pursuant to the Installment Sale Agreement.

“Securities Depositories” means: The Depository Trust Company, 711 Stewart Avenue, Garden City, New York 11530, Fax (516) 227-4039 or 4190: and, in accordance with then current guidelines of the Securities and Exchange Commission, such other addresses as such depositories may specify and/or such other securities depositories as the District may designate in a Written Request of the District delivered to the Trustee.

“Special Counsel” or “Bond Counsel” means Best Best & Krieger LLP, or a firm of nationally recognized attorneys experienced in the issuance of obligations the interest on which is excluded from gross income for purposes of Section 103 of the Code, which firm is selected by the District.

“S&P” means Standard & Poor’s Ratings Group, a corporation organized and existing under and pursuant to the laws of the State of New York, and its successors and assigns, except that if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, then the term “S&P” shall be deemed to refer to any other nationally recognized securities rating agency selected by the District upon written notice to the Trustee and the Bank.

“State” means the State of California.

“Stated Amount” means the maximum aggregate amount available to be drawn under the Facility, which initially shall be \$15,572,142.47 as from time to time decreased and/or increased in accordance with the term of the Facility.

“Stated Maturity” when used with respect to any Certificate or any installment of interest thereon means the date specified in such Certificate as the fixed date on which the principal of such Certificate or such installment of interest is due and payable.

“Statement of the District or the Corporation” means, as applicable, a statement signed by or on behalf of (i) the Corporation by its President or a Vice President, or (ii) by the District by the Chairman of its Board of Directors or General Manager or by any other person who is specifically authorized by resolution of the Board of Directors of the District to sign or execute such a document on its behalf. If and to the extent required by the provisions of the Trust Agreement, each Statement of the Corporation or District shall include the statements provided for in the Trust Agreement.

“Substitute Facility” means a facility meeting the requirements set forth in the Trust Agreement.

“Tax Revenue Fund” means the fund by that name established under the Installment Sale Agreement.

“Taxes” means all taxes, including *ad valorem* taxes of the District, other than taxes imposed pursuant to Chapter 1 of Part 9 of the Law to secure general obligation bonds of the District or any improvement district thereof;

“Tender Agent” means the Bank of New York Mellon Trust Company, as Tender Agent under the Tender Agreement or any successor thereto.

“Tender Agreement” means the tender agent agreement dated as of June 1, 1996 by and between the District and the Tender Agent, as amended.

“Term” means the period commencing upon the effective date of the Installment Sale Agreement and ending upon the sooner to occur of (i) September 1, 2026; and (ii) the payment by the District of all amounts due under the Installment Sale Agreement; provided that notwithstanding the foregoing the Term shall not end prior to payment by District of all amounts due hereunder, including all amounts due to the Bank.

“Termination Date” means June 30, 2014, the stated expiration date of the Facility as such date may be extended, or any earlier date on which the Facility or Substitute Facility shall terminate, expire or be canceled.

“Trust Agreement” means the Trust Agreement by and among the District, the Corporation and the Trustee, dated as of July 1, 1996, as originally executed or as it may be amended from time to time as provided therein, including as amended by a First Supplement to Trust Agreement by and among the District, the Corporation and the Trustee, dated as of May 25, 2011.

“Water System” means all properties and assets, real and personal, tangible and intangible, of the District now or hereafter existing, used or pertaining to the production, treatment, transmission, distribution and sale of water, including all additions, extensions, expansions, improvements and betterments thereto, and equipments thereof; provided, however, that to the extent the District is not the sole owner of an asset or property, only the District’s ownership interest in such asset or property shall be considered a part of its Water System.

“Written Consent of the Corporation or District,” “Written Order of the Corporation or District,” “Written Request of the Corporation or District,” and “Written Requisition of the Corporation or District” mean, respectively, a written consent, order, request or requisition signed by or on behalf of (i) the Corporation by its President or a Vice President or (ii) the District by the Chairman of its Board of Directors or General Manager or by any person who is specifically authorized by resolution of the Board of Directors of the District to sign or execute such a document on its behalf.

## TRUST AGREEMENT

### CERTIFICATES; TERMS AND PROVISIONS

Transfer of Certificates. Any Certificate may, in accordance with its terms, be transferred upon the books required to be kept pursuant to the provisions of the Trust Agreement by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such Certificate for cancellation, accompanied by delivery of a written instrument of transfer in a form acceptable to the Trustee, duly executed. Transfer of any Certificate shall not be permitted by the Trustee (i) if the Trustee has received written notice from the Tender Agent during any Variable Rate Period that it has received notice from the Owner of such Certificate that such Certificate will be delivered to the Tender Agent for purchase on or before the next succeeding Interest Payment Date, (ii) during the fifteen (15) day period prior to the date designated by the Trustee for the selection of Certificates for prepayment, or (iii) if such Certificate has been called for prepayment or is then subject to mandatory tender pursuant to the Trust Agreement.

Whenever any Certificate shall be surrendered for transfer, the Trustee shall execute and shall deliver a new Certificate for a like aggregate principal amount of authorized denominations. The Trustee shall require the Certificate Owner requesting such transfer to pay any tax or other governmental charge required to be paid with respect to such transfer, and may in addition require the payment of a reasonable sum to cover expenses incurred by the District or the Trustee in connection with such transfer.

Exchange of any Certificate shall not be permitted by the Trustee (a) if the Trustee has received written notice from the Tender Agent during any Variable Rate Period that it has received notice from the Owner of such Certificate that such Certificate will be delivered to the Tender Agent for purchase on or before the next succeeding Interest Payment Date, (b) during the fifteen (15) day period prior to the date designated by the Trustee for the selection of Certificates for prepayment, or (c) if such Certificate has been called for prepayment or is then subject to mandatory tender pursuant to the Trust Agreement.

### VALIDITY OF CERTIFICATES

Validity of Certificates. The validity of the execution and delivery of the Certificates is not dependent on and shall not be affected in any way by any proceedings taken by the District, the Corporation or the Trustee with respect to or in connection with the Installment Sale Agreement. The recital contained in the Certificates that all acts, conditions and things required by the Constitution and statutes of the State of California and the Trust Agreement to exist, to have happened and to have been performed precedent to and in the delivery thereof do exist, have happened and have been performed in due time, form and manner as required by law shall be conclusive evidence of their validity and of compliance with the provisions of law in their delivery.

## INSTALLMENT PAYMENTS; FACILITY; SUBSTITUTE FACILITY

Deposit of Installment Payments. All Installment Payments to which the Corporation may at any time be entitled (including income or profit from investments), deposited by the District in the Installment Payment Fund pursuant to the Installment Sale Agreement, shall be paid directly to the Trustee pursuant to the terms of the Trust Agreement, and if received by the Corporation at any time shall be deposited by the Corporation with the Trustee within one Business Day after the receipt thereof, and the Trustee shall deposit all Installment Payments as and when received in the Certificate Payment Fund. All moneys at any time deposited in the Certificate Payment Fund shall be held by the Trustee in trust for the benefit of the Owners from time to time of the Certificates, and for the benefit of the Bank as provided in the Trust Agreement, but shall nevertheless be disbursed, allocated and applied solely for the uses and purposes set forth in the Trust Agreement.

Certificate Payment Fund. There is established with the Trustee the Certificate Payment Fund consisting of a District Payments Account and a Debt Service Account, which the Trustee covenants to maintain and hold in trust separate and apart from other funds held by it so long as any Installment Payments remain unpaid. The Trustee shall transfer from the Certificate Payment Fund the following amounts at the times and in the manner hereinafter provided, and shall deposit such amounts in one or more of the following respective accounts, each of which the Trustee shall establish and maintain and hold in trust separate and apart from other funds held by it, and each of which shall be disbursed and applied only as authorized in the Trust Agreement. Such amounts shall be so transferred to and deposited in the following respective Accounts:

1. All amounts paid by the District as Installment Payments shall be deposited in the District Payments Account. The Trustee shall also deposit to the Certificate Payment Fund all amounts required to be deposited thereunder in accordance with the Trust Agreement. The Trustee shall, in accordance with the Trust Agreement, make the necessary drawings under the Facility to pay the amounts specified in the Trust Agreement and deposit such amounts in the Debt Service Account. Subject to paragraph (b) below, the amounts on deposit in the Certificate Payment Fund shall be used solely for the payment of principal, mandatory prepayment, interest or the Purchase Price of the Certificates. After the Fixed Rate Conversion Date, on each date on which any payment of principal, mandatory prepayment, or interest is due with respect to the Certificates, the Trustee shall withdraw from the District Payments Account of the Certificate Payment Fund for application to payment of such debt service an amount equal to the debt service due on such Certificates on such date.

2. On each day on which the Trustee has received money drawn on the Facility in the amount specified in the Trust Agreement, the Trustee shall, not later than 4:00 p.m., New York City time, wire transfer to the Bank's account as specified in writing by the Bank from funds on deposit in the District Payments Account, if any, an amount equal to the amounts so drawn under the Facility. Notwithstanding anything to the contrary contained herein, in the event the Bank fails to honor a draw on the Facility in accordance with its terms, the Trustee shall pay the principal, prepayment price or interest due with respect to the Certificates from any Installment Payments on deposit in the District Payments Account regardless of whether such Installment Payments constitute Eligible Funds.

Surplus. Any surplus remaining in the Certificate Payment Fund, after prepayment and payment of all Certificates, including premiums (if any) and accrued interest, and payment of any applicable draws, accrued interest, fees and expenses to the Trustee and the Bank or provision for such prepayment and payment having been made to the satisfaction of the Trustee and the Bank, shall be withdrawn by the Trustee and remitted to the District.

Facility. The Trustee shall hold and maintain the Facility for the benefit of the Certificate Owners until the expiration date thereof. The Trustee shall diligently enforce all terms, covenants and conditions of the Facility, including payment when due of any use of the Facility, and will not consent to or agree to or permit any amendment or modification of the Facility which would materially adversely affect the rights or security of the Owners of the Certificates. If at any time during the term of the Facility, any successor Trustee shall be appointed and qualified under the Trust Agreement, the resigning or removed Trustee shall request that the Bank transfer the Facility to the successor Trustee. If the resigning or removed Trustee fails to make this request, the successor Trustee shall do so before accepting appointment. When any Facility expires in accordance with its terms or is replaced by a Substitute Facility, the Trustee shall immediately surrender such Facility to the issuing Bank.

In accordance with its terms, the Facility may be terminated as herein provided. The original Facility and any Substitute Facility shall be an obligation of the Bank to pay to the Trustee upon request made with respect to the Certificates related thereto and in accordance with the terms thereof:

(a) An amount, not exceeding the aggregate principal amounts of the Certificates, sufficient to pay the principal portion of the Purchase Price of the Certificates delivered or required to be delivered to the Tender Agent for purchase, or the principal amount of Certificates when due at their Stated Maturity or upon mandatory redemption or acceleration; and

(b) An amount, not exceeding interest on the Certificates for 34 days computed at the Maximum Rate, sufficient to pay the interest portion of the Purchase Price of Certificates delivered to the Tender Agent for purchase, or the interest accrued with respect to Certificates when due at their Stated Maturity or upon mandatory redemption, optional redemption or acceleration.

If a Facility is in effect with respect to the Certificates, the Trustee shall make a drawing under the Facility (in the manner and to the extent therein permitted) in an amount sufficient, and by the time required, to timely pay the principal of, interest on and the Purchase Price of the Certificates to become due at the Maturity thereof (upon their Stated Maturity, mandatory redemption, optional redemption or acceleration), or to timely pay the interest with respect to the Certificates to become due on each Interest Payment Date and Purchase Date, but in every case only in respect of Certificates which are not Bank Certificates, and the Trustee shall deposit the funds received from such a draw on the Facility in the Debt Service Account of the Certificate Payment Fund; provided, however, that, in the case of a prepayment of Certificates pursuant to the Trust Agreement, the Trustee shall not be required to present a draw under the Facility to the extent that the Trustee holds other Eligible Funds pursuant to the Trust Agreement in an amount sufficient to pay the Prepayment Price of the Certificates selected for prepayment on the prepayment date, and provided further that no draw shall be made under the Facility to pay the premium, if any, on the Certificates selected for prepayment. Without limiting the generality of the foregoing, at such time as the duration of the Rate Period is greater than one (1) month in duration, the Trustee is hereby instructed to draw upon the Facility on the first day of each calendar month during such Rate Period, commencing with the first day of the second month of such Rate Period (or on the Business Day preceding the first day of each such month, in the event such day is not a Business Day), an amount equal to the interest with respect to the Certificates that has accrued (or will accrue) during the month for which the drawing is being submitted, less, with respect to the final drawing of the Rate Period, investment earnings (if any) on any previous amounts drawn under the Facility, which investment earnings are on deposit in the Debt Service Account. All moneys held by the Trustee from draws on the Facility shall be held uninvested or, upon written direction of the District be, invested in non-callable, non-prepayable Federal Securities which mature not later than next Business Day. Notwithstanding the deposit of such moneys under the Trust Agreement and the subsequent reimbursement to the Bank, the District shall have no right, title or interest in such moneys and such moneys will be held exclusively for the Holders of the Certificates and paid over in accordance with the provisions of the Trust Agreement.

Payments of the principal of and interest with respect to Certificates representing interest at Variable Rates or CP Rates, whether at their Stated Maturity or upon their prepayment or acceleration, shall be made by the Trustee from the following sources in the order of priority indicated:

- (1) moneys paid to the Trustee from drawings under the Facility;
- (2) other Eligible Funds; and
- (3) any other moneys deposited by the District pursuant to the Installment Sale Agreement.

Upon and following the conversion of the Certificates to the Fixed Rate, the Certificates shall no longer be payable from or secured by the Facility or subject to tender for purchase.

Substitute Facility. If at any time the District shall deliver to the Trustee (1) a Substitute Facility, (2) an opinion of counsel stating that the delivery of such Substitute Facility to the Trustee is authorized under the Trust Agreement and complies with the terms hereof, (3) an Opinion of Bond Counsel that the proposed substitution will not adversely affect the exclusion of interest on the Certificates from gross income for federal income tax purposes, (4) one or more opinions of counsel addressed to the Trustee, to the effect, singly or together, that: (A) the Substitute Facility is a legal, valid and binding obligation of the obligor, enforceable against the obligor in accordance with its terms, except as limited by applicable reorganization, insolvency, liquidation, readjustment of debt, moratorium or other similar laws affecting the enforcement of the rights of creditors generally as such laws may be applied in the event of a reorganization, insolvency, liquidation, readjustment of debt or other similar proceeding of or moratorium applicable to the obligor and by general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law); and (B) payments made by the obligor under the Substitute Facility will not be voidable under Section 547 of the United States Bankruptcy Code in the context of a case or proceeding by or against the District or any Affiliates thereof under the United States Bankruptcy Code; (5) if a rating or ratings on the Certificates shall be in effect on the date of such substitution, written evidence from Moody's and/or Standard & Poor's, as applicable, to the effect that such rating agency has reviewed the proposed Substitute Facility and that the substitution of the proposed Substitute Facility for the existing Facility will not, by itself, result in a reduction or withdrawal of its rating on the Certificates, and (6) written evidence that notice of such proposed substitution has been sent to the Owners prior to such substitution, then the Trustee shall, so long as such Substitute Facility shall contain administrative procedures which are acceptable to the Trustee in its reasonable discretion, accept such Substitute Facility and promptly surrender the existing Facility to the issuer thereof.

Alternatively, if all of the requirements of the preceding paragraph are satisfied other than those set forth in clause (5) thereof, and the District has given the Trustee at least forty-five (45) days' written notice of its intention to substitute such Facility and simultaneously with such written notice the Trustee, the Remarketing Agent and the Tender Agent receive an Opinion of Bond Counsel to the effect that the substitution will not adversely affect the exclusion of the interest on the Certificates from gross income for federal income tax purposes, the Trustee shall accept the Substitute Facility, enforce payment of any amounts due under the existing Facility to the extent required by the Trust Agreement and thereupon surrender the existing Facility.

Any Substitute Facility shall be an irrevocable purchase agreement, letter of credit, surety bond, insurance policy, guaranty or other irrevocable credit facility, or any combination thereof, issued by one or more commercial banks or savings and loan associations, insurance companies or other financial institutions, the terms of which shall in all respects material to the interests of the Owners be the same as the Facility, except that the expiration date of such Substitute Facility may be later than the expiration date for the existing Facility and such expiration date shall be not less than one (1) year after the date such Substitute Facility is substituted for the existing Facility.

Investment of Moneys in Special Fund. Any moneys in the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account shall be invested by the Trustee upon the Written Request of the District, in Permitted Investments which will mature on or before the dates when such moneys are scheduled to be needed for payment from such fund and in accordance with the limitations set forth in the Trust Agreement, provided that moneys resulting from a draw on the Facility shall be invested solely in non-callable, non-prepayable Federal Securities maturing not later than the next business day or remain uninvested. Securities acquired as an investment of moneys in a fund shall be credited to such fund. Such Written Request of the District shall certify that the investment is a Permitted Investment.

In the absence of written investment direction from the District, the Trustee shall invest moneys held by it solely in Permitted Investments specified in clause (8) of the definition thereof unless otherwise directed in the Trust Agreement.

Such investments shall be valued by the Trustee as frequently as deemed necessary by the Bank, but not less often than semiannually, as set forth below, at the market value thereof, exclusive of accrued interest. Deficiencies in the amount on deposit in any fund or account resulting from a decline in market value shall be restored no later than the succeeding valuation date.

Any interest, profit or other income on such investments shall be deposited in the Certificate Payment Fund established under the Trust Agreement.

Subject to the further provisions of the Trust Agreement, the Trustee may sell or present for prepayment any obligations so purchased at the direction of the District whenever it shall be necessary in order to provide moneys to meet any payment, and the Trustee shall not be liable or responsible for any loss resulting from such investment. The Trustee and its affiliates may act as sponsor, advisor, depository, principal or agent in the acquisition or disposition of any investment and receive compensation in connection therewith. The Trustee may commingle any of the funds or accounts established pursuant to the Trust Agreement into a separate fund or funds for investment purposes only; provided, however, that all funds or accounts held by the Trustee hereunder shall be accounted for separately notwithstanding such commingling.

Pledge of Moneys in Funds. All amounts on deposit in the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account are irrevocably pledged to the Owners of the Certificates and the Bank as provided in the Trust Agreement. This pledge shall constitute a first and exclusive lien on the Certificate Payment Fund, the Debt Service Account, the District Payments Account and the Prepayment Account for the benefit of the Owners of the Certificates in accordance with the terms of the Trust Agreement and of the Installment Sale Agreement.

Corporation and District to Perform Installment Sale Agreement. The Corporation and District covenant and agree with the Owners of the Certificates to perform all obligations and duties imposed on them under the Installment Sale Agreement and, together with the Trustee, to enforce such Installment Sale Agreement against the other party thereto in accordance with its terms.

The Corporation and the District will in all respects promptly and faithfully keep, perform and comply with all the terms, provisions, covenants, conditions and agreements of the Installment Sale Agreement to be kept, performed and complied with by it.

The Corporation and the District agree not to do or permit anything to be done, or omit or refrain from doing anything, in any case where any such act done or permitted to be done, or any such omission of or refraining from action, would or might be a ground for cancellation or termination of the Installment Sale Agreement.

Tax Covenants. The Corporation and the District covenant with the Owners of the Certificates that, notwithstanding any other provision of the Trust Agreement, they will make no use of the proceeds of the Certificates that would cause the Certificates to be “arbitrage bonds” within the meaning of Section 148 of the Code.

The District will not make any use of the proceeds of the Certificates or any other funds of the District, or take or omit to take any other action, that would cause the Certificates to be “private activity bonds” within the meaning of Section 141 of the Code, or “federally guaranteed” within the meaning of Section 149(b) of the Code. To that end, so long as any Installment Payments are unpaid, the District, with respect to such proceeds and such other funds, will comply with all requirements of such Sections and all regulations of the United States Department of the Treasury issued thereunder and under Section 103 of the Internal Revenue Code of 1954, as amended, to the extent such requirements are, at the time, applicable and in effect.

The District will not use or permit the use of the Project or any portion thereof by any person other than a governmental unit as such term is used in Section 141 of the Code, in such manner or to such extent as would result in the loss of exclusion from gross income for federal income tax purposes of the portion of the Installment Payments constituting interest under Section 103 of the Code.

Accounting Records and Reports. The Trustee shall keep or cause to be kept proper books of record and account in which complete and correct entries shall be made of all transactions made by it relating to the receipts, disbursements, allocation and application of the Installment Payments, and such books shall be available for inspection by the District and by any Owner of Certificates, or his agent or representative, at reasonable hours and under reasonable conditions. Each month, so long as the Certificates are Outstanding, the Trustee shall furnish to the District a statement covering receipts, disbursements, allocation and application of amounts on deposit in the funds and accounts created hereunder held by it.

Compliance with Trust Agreement. The Trustee will not execute, or permit to be executed, any Certificates in any manner other than in accordance with the provisions of the Trust Agreement, and the District will not suffer or permit any default by it to occur under the Trust Agreement, but will faithfully observe and perform all the covenants, conditions and requirements hereof.

Observance of Laws and Regulations. To the extent necessary to assure their performance hereunder, the Corporation and the District will well and truly keep, observe and perform all valid and lawful obligations or regulations now or hereafter imposed on them by contract, or prescribed by any law of the United States of America, or of the State, or by any officer, board or commission having jurisdiction or control, as a condition of the continued enjoyment of any and every right, privilege or franchise now owned or hereafter acquired by the Corporation or the District, respectively, including its right to exist and carry on its business, to the end that such contracts, rights and franchises shall be maintained and preserved, and shall not become abandoned, forfeited or in any manner impaired.

Liens. So long as any Certificates are Outstanding, neither the District nor the Trustee, as assignee of the Corporation, will create or suffer to be created any pledge of or lien on the Installment Payments.

Prosecution and Defense of Suits. The Trustee, as assignee of the Corporation, to the extent indemnified by the District through the payment of Additional Costs under the Installment Sale Agreement, will defend against every action, suit or other proceeding at any time brought against the Trustee or any Owner upon any claim arising out of the receipt, deposit or disbursement of any of the Installment Payments or involving the rights of any Owner hereunder provided that the Trustee shall in no event be obligated to defend any such action, suit or proceeding if the District fails to indemnify the Trustee through the payment of Additional Costs under the Installment Sale Agreement or if such payment of Additional Costs is for any reason not made available to the Trustee; provided, further, that the Trustee

or any Owner at its or his election and at its or his sole cost and expense may appear in and defend any such action, suit or other proceeding.

Recordation and Filing. The District (pursuant to the Installment Sale Agreement) shall record, register, file, renew, refile and rerecord all such documents, including financing statements, as may be required by law in order to maintain a security interest in the Trust Agreement, the Installment Payments and Net Revenues, all in such manner, at such times and in such places as may be required by, and to the extent permitted by, law in order fully to preserve, protect and perfect the security of the Certificate Owners and the rights and security interests of the Trustee. The District shall (subject to the preceding paragraph) do whatever else may be necessary or be reasonably required in order to perfect and continue the lien of the Trust Agreement.

Further Assurances. Whenever and so often as requested so to do by the Trustee, Bank or any Certificate Owner, the Corporation and the District will promptly execute and deliver or cause to be executed and delivered all such other and further instruments, documents or assurances, and promptly do or cause to be done all such other and further things, as may be necessary or reasonably required in order to further and more fully vest in the Trustee and the Certificate Owners all rights, interest, powers, benefits, privileges and advantages conferred or intended to be conferred upon them by the Trust Agreement.

#### DEFAULT AND LIMITATION OF LIABILITY

Notice of Non-Payment. In the event of delinquency in the payment of any Installment Payments due by the District pursuant to the Installment Sale Agreement, the Trustee shall, after one Business Day following the date upon which such delinquent Installment Payment was due, immediately give written notice of the delinquency and the amount of the delinquency to the District, the Corporation and the Bank and notice of any other Event of Default within 30 days of knowledge thereof.

Action on Default or Termination. Upon the occurrence of an Event of Default, which shall also constitute a default under the Trust Agreement, and in each and every such case during the continuance of such Event of Default, the Trustee may exercise or shall if indemnified to its satisfaction exercise, as the case may be, any and all remedies available pursuant to law or granted pursuant to the Installment Sale Agreement. In determining whether a payment default has occurred or whether a payment on the Certificates has been made under the Trust Agreement, no effect shall be given to payments made under the Facility. The Trustee shall not take the Facility into account in determining whether the rights of Certificate holders are adversely affected by actions taken pursuant to the terms and provisions of the Trust Agreement or the Installment Sale Agreement; provided, however, that the Trustee shall not be able to require indemnification prior to an acceleration of the Certificates and the Installment Payments resulting from an Event of Default described in the Installment Sale Agreement the making a draw under the Facility or making a payment to the Holders of the Certificates.

The Bank shall be included as a party in interest and as a party entitled to (i) notify the Trustee of the occurrence of an Event of Default, and (ii) request the Trustee to intervene in judicial proceedings that affect the Certificates or the security therefor. The Trustee shall accept notice of default from the Bank.

Additionally, the Owners of Certificates, the Trustee on behalf of the Owners and the District shall have the right to bring suit, or exercise any other remedy available pursuant to law against the Bank to enforce any obligation of the Bank should it fail to perform any of its obligations under the Trust Agreement or under the Facility.

Anything in the Trust Agreement to the contrary notwithstanding, upon the occurrence and continuance of an Event of Default as defined therein, the Bank shall be entitled to control and direct the enforcement of all rights and remedies granted to the Certificate Owners or the Trustee for the benefit of the Certificate Owners under the Trust Agreement, including, without limitation: (i) the right to accelerate the principal of the Certificates (except with respect to an Event of Default which occurs as the result of the

receipt by the Trustee of written notice from the Bank that it has not reinstated the interest component of the Facility) as described in the Trust Agreement, and (ii) the right to annul any declaration of acceleration, and the Bank shall also be entitled to approve all waivers of Events of Default.

Upon the occurrence of an Event of Default, the Trustee may, with the consent of the Bank, and shall, at the direction of the Bank or 50% of the Certificate Owners with the consent of the Bank, by written notice to the District and the Bank, declare the principal of the Certificates to be immediately due and payable, whereupon that portion of the principal of the Certificates thereby coming due and the interest thereon accrued to the date of payment shall, without further action, become and be immediately due and payable, anything in the Trust Agreement or in the Certificates to the contrary notwithstanding.

Upon declaration of the entire principal amount of the unpaid Installment Payments and the accrued interest thereon to be due and payable immediately and provided such declaration is not rescinded or annulled, all in accordance with the Installment Sale Agreement, the Trustee may apply all moneys received as Installment Payments and all moneys held in any fund or account hereunder (other than the Rebate Fund) in the manner provided in the Trust Agreement. Upon declaration of an acceleration, interest on the Certificates shall cease to accrue.

Application of Moneys Collected by Trustee. Any moneys collected (excluding moneys drawn under the Facility) by the Trustee pursuant to the Trust Agreement after an Event of Default has occurred shall be applied in the order following, at the date or dates fixed by the Trustee and, in the case of distribution of such moneys on account of principal (or premium, if any) or interest, upon presentation of the Certificates, and stamping thereon the payment, if only partially paid, and upon surrender thereof, if fully paid:

First: To the payment of all costs and expenses of collection, just and reasonable compensation to the Trustee for its own services and for the services of counsel, agents and employees by it properly engaged and employed, and all other expenses and liabilities incurred, pursuant to the provisions of the Trust Agreement, together with interest on all such amounts advanced by the Trustee at the highest rate permitted by law.

Second: In case the principal of none of the Certificates shall have become due and remains unpaid, to the payment of interest in default, such payments to be made ratably and proportionately to the persons entitled thereto.

Third: In case the principal of the Certificates shall have become due by acceleration or otherwise and remains unpaid, first to the payment of interest in default and then to the payment of principal of the Certificates then due and unpaid, in every instance such payment to be made ratably to the persons entitled thereto.

Fourth: Additional Costs.

If such moneys are invested, they shall be invested only in Permitted Investments having a maturity of thirty (30) days or less.

Other Remedies of the Trustee. The Trustee, with the consent of the Bank, and upon being indemnified to its satisfaction therefor, in its discretion may:

1. by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the District or any director, officer or employee thereof, and to compel the District or any such director, officer or employee to perform or carry out its or his duties under law and the agreements and covenants required to be performed by it or him contained in the Trust Agreement;

2. by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

3. by suit in equity upon the happening of any default hereunder to require the District and its directors, officers and employees to account as the trustee of an express trust.

Trustee to Represent Owners. The Trustee is irrevocably appointed (and the successive respective Owners of the Certificates by taking and holding the same, shall be conclusively deemed to have so appointed the Trustee) as trustee and true and lawful attorney in fact of the Owners of the Certificates for the purpose of exercising and prosecuting on their behalf such rights and remedies as may be available to such Owners under the provisions of the Certificates, the Trust Agreement, the Installment Sale Agreement and applicable provisions of law. Upon the occurrence and continuance of an event of default or other occasion giving rise to a right in the Trustee to represent the Owners, the Trustee in its discretion may, and upon the written request of the Owners of not less than twenty-five percent (25%) in aggregate principal amount of the Certificates then Outstanding, and upon being indemnified to its satisfaction therefor, shall, proceed to protect or enforce its rights or the rights of such Owners by such appropriate action, suit, mandamus or other proceedings as it shall deem most effectual to protect and enforce any such right, at law or in equity, either for the specific performance of any covenant or agreement contained herein, or in aid of the execution of any power herein granted, or for the enforcement of any other appropriate legal or equitable right or remedy vested in the Trustee or in such Owners under the Trust Agreement, the Installment Sale Agreement or any law; and upon instituting such proceeding, the Trustee shall be entitled, as a matter of right, to the appointment of a receiver of the Net Revenues and other assets pledged under the Trust Agreement pending such proceedings. All rights of action under the Trust Agreement or the Certificates or otherwise may be prosecuted and enforced by the Trustee without the possession of any of the Certificates or the production thereof in any proceeding relating thereto, and any such suit, action or proceeding instituted by the Trustee shall be brought in the name of the Trustee for the benefit and protection of all the Owners of such Certificates, subject to the provisions of the Trust Agreement.

Owners' Direction of Proceedings. Subject to the rights of the Bank to control proceeding in the Trust Agreement, the Owners of a majority in aggregate principal amount of the Certificates then Outstanding shall have the right, by an instrument or concurrent instruments in writing executed and delivered to the Trustee, together with indemnity satisfactory to the Trustee, to direct the method of conducting all remedial proceedings taken by the Trustee under the Trust Agreement, provided that such direction shall not be otherwise than in accordance with law and the provisions of the Trust Agreement, and that the Trustee shall have the right to decline to follow any such direction which in the opinion of the Trustee would be unjustly prejudicial to Owners of Certificates not parties to such direction or may result in individual liability for the Trustee. The Trustee shall not be liable for any actions performed at the direction of the Owners of the Certificates given pursuant to the Trust Agreement.

No Owner of any Certificate shall have the right to institute any such action or proceeding at law or in equity, for the protection or enforcement of any right or remedy under the Trust Agreement, the Installment Sale Agreement or any applicable law with respect to such Certificate, unless (1) such Owner shall have given to the Trustee written notice of the occurrence of an Event of Default; (2) the Owners of not less than 25% in aggregate principal amount of the Certificates then Outstanding shall have made written request upon the Trustee to exercise the powers granted or to institute such suit, action or proceeding in its own name; (3) such Owner or said Owners shall have tendered to the Trustee reasonable indemnity against the costs, expenses and liabilities to be incurred in compliance with such request; and (4) the Trustee shall have refused or omitted to comply with such request for a period of sixty (60) days after such written request shall have been received by, and said tender of indemnity shall have been made to, the Trustee.

Such notification, request, tender of indemnity and refusal or omission are hereby declared, in every case, to be conditions precedent to the exercise by any Owner of Certificates of any remedy under the Trust Agreement or under law; it being understood and intended that no one or more Owners of Certificates shall have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Trust Agreement or the rights of any other Owners of Certificates, or to enforce any right under the Trust Agreement, the Installment Sale Agreement or other applicable law with respect to the Certificates, except in the manner therein provided, and that all proceedings at law or in equity to enforce any such right shall be instituted, had and maintained in the manner herein provided and for the benefit and protection of all Owners of the Outstanding Certificates, subject to the provisions of the Trust Agreement.

Notwithstanding any other provision in the Trust Agreement, each Owner shall have the right to receive payment of the principal and the premium, if any, and interest represented by its Certificate at the respective dates on which the same became due and payable in accordance with the terms, from the source and in the manner provided in such Certificate and in the Trust Agreement, and to institute suit for the enforcement of any such payment, and such rights shall not be impaired without the consent of such Owner.

Non-Waiver. A waiver of any default or breach of duty or contract by the Trustee shall not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent default or breach of duty or contract. No delay or omission by the Trustee or the Owners of the Certificates to exercise any right or remedy accruing upon any default or breach of duty or contract shall impair any such right or remedy or shall be construed to be a waiver of any such default or breach of duty or contract or an acquiescence therein, and every right or remedy conferred upon the Trustee by law or by this article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the Trustee or the Owners of the Certificates, the Trustee, the Owners of the Certificates and the District shall be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Trust Agreement conferred upon or reserved to the Trustee or the Owners of the Certificates is intended to be exclusive of any other remedy, and each such remedy shall be cumulative and shall be in addition to every other remedy given under the Trust Agreement or now or hereafter existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by any law.

No Obligation of the District to the Owners. Except for the payment of Installment Payments when due in accordance with the Installment Sale Agreement and the performance of the other covenants and agreements of the District contained in said Installment Sale Agreement and in the Trust Agreement, the District shall have no obligation or liability to the Owners of the Certificates with respect to the Trust Agreement or the execution, delivery or transfer of the Certificates, or the disbursement of Installment Payments to the Owners by the Trustee; provided however that nothing contained in this paragraph shall affect the rights, duties or obligations of the Trustee expressly set forth in the Trust Agreement.

No Obligation with Respect to Performance by Trustee. Neither the District nor the Corporation shall have any obligation or liability to any of the other parties to the Trust Agreement or to the Owners of the Certificates with respect to the performance by the Trustee of any duty imposed upon it under the Trust Agreement.

No Liability to Owners for Payment. The Corporation shall not have any obligation or liability to the Owners of the Certificates with respect to the payment of the Installment Payments by the District when due, or with respect to the performance by the District of any other covenant made by it in the Installment Sale Agreement or in the Trust Agreement. Except as provided in the Trust Agreement, the Trustee shall not have any obligation or liability to the Owners of the Certificates with respect to the payment of the Installment Payments by the District when due, or with respect to the performance by the District of any other covenant made by it in the Installment Sale Agreement or in the Trust Agreement.

No Responsibility for Sufficiency. The Trustee shall not be responsible for the sufficiency of the Trust Agreement, the Installment Sale Agreement, or of the assignment made to it under the Trust Agreement of rights to receive Installment Payments pursuant to the Installment Sale Agreement, or the value of or title to the Project. The Trustee shall not be responsible or liable for any loss suffered in connection with any investment of funds made by it under the terms of and in accordance with the Trust Agreement.

#### AMENDMENT OF TRUST AGREEMENT

Amendments Permitted. The Trust Agreement and the rights and obligations of the District and of the Owners of the Certificates and of the Trustee may be modified or amended at any time by an amendment thereto which shall become binding when the written consents of the Bank and the Owners of a majority in aggregate principal amount of the Certificates then Outstanding, exclusive of Certificates disqualified as provided in the Trust Agreement, shall have been filed with the Trustee and the Bank. No such modification or amendment shall (1) extend the stated maturities of the Certificates, or reduce the rate of interest represented thereby, or extend the time of payment of interest, or reduce the amount of principal represented thereby, or reduce any premium payable on the prepayment thereof, or impair the right of any Owner to tender such Owner's Certificate as provided for in the Trust Agreement, without the consent of the Owner of each Certificate so affected, or (2) reduce the aforesaid percentage of Owners of Certificates whose consent is required for the execution of any amendment or modification of the Trust Agreement, or (3) modify any of the rights or obligations of the Trustee, the Bank or the District without its written consent thereto.

The Trust Agreement and the rights and obligations of the Corporation, the Trustee, the District and of the Owners of the Certificates may also be modified or amended at any time by an amendment thereto which shall become binding upon execution and receipt of the written consent of the Bank but without the consent of the Owners of any Certificates, but only to the extent permitted by law and only for anyone or more of the following purposes:

- (1) to add to the covenants and agreements of the Corporation or the District contained in the Trust Agreement other covenants and agreements thereafter to be observed or to surrender any right or power herein reserved to or conferred upon the Corporation or the District, and which shall not adversely affect the interests of the Owners of the Certificates;
- (2) to cure, correct or supplement any ambiguous or defective provision contained in the Trust Agreement or in regard to questions arising under the Trust Agreement, as the Corporation or the District may deem necessary or desirable and which shall not adversely affect the interests of the Owners of the Certificates;
- (3) to provide, if necessary, for more than one financial institution or insurance company to be the issuer of the Facility as permitted in the Trust Agreement; and
- (4) to make such other amendments or modifications as may be necessary in order to obtain a rating on the Certificates from Standard & Poor's Corporation, Moody's Investors Service or any other nationally recognized rating services or which otherwise may be in the best interests of the Owners of the Certificates.

The Trustee shall have received an opinion of Special Counsel to the effect that such amendment or modification will not adversely affect the exclusion from gross income, for purposes of Section 103 of the Code, of interest on the Certificates.

Endorsement or Replacement of Certificates After Amendment or Supplement. After the effective date of any action taken as provided in the Trust Agreement, the Trustee may determine that the Certificates may bear a notation by endorsement in form approved by the Trustee as to such action, and in that case upon demand of the Trustee to the Owner of any Outstanding Certificate and presentation of such Owner's Certificate for such purpose at the principal corporate trust office of the Trustee a suitable notation as to such action shall be made on such Certificate. If the Trustee shall so determine, new Certificates so modified as in the opinion of the Trustee shall be necessary to conform to such action shall be prepared, and in that case upon demand of the Trustee to the Owner of any Outstanding Certificates such new Certificates shall be exchanged at the principal corporate trust office of the Trustee without cost to each Owner for Certificates then Outstanding upon surrender of such Outstanding Certificates.

Amendment of Particular Certificates. The provisions of the Trust Agreement will not prevent any Owner from accepting any amendments to the particular Certificates held by him, provided that due notation thereof is made on such Certificates.

#### DEFEASANCE

Discharge of Trust Agreement. When the obligations of the District under the Installment Sale Agreement shall cease pursuant to the Installment Sale Agreement (except for the right of the Trustee and the obligation of the District to have the Eligible Funds and Permitted Investments mentioned therein applied to the payment of Installment Payments as therein set forth and the obligation to apply moneys on deposit in the Rebate Fund), then in that case the obligations created by the Trust Agreement shall thereupon cease, terminate and become void except for the obligation of the District to direct the Trustee to apply money on deposit in the Rebate Fund as provided in the Trust Agreement which shall continue until such moneys are so applied and the right of the Owners to have applied and the obligation of the Trustee to apply such Eligible Funds and Permitted Investments to the payment of the Certificates as set forth in the Trust Agreement and, subject to application of moneys on deposit in the Rebate Fund, the Trustee shall turn over to the District, after provision for payment of amounts due the Trustee thereunder, as an overpayment of Installment Payments, any surplus in the Certificate Payment Fund and all balances remaining in any other funds or accounts other than moneys and Permitted Investments held for the payment of the Certificates at maturity or on prepayment, which moneys and Permitted Investments shall continue to be held by the Trustee in trust for the benefit of the Owners and shall be applied by the Trustee to the payment, when due, of the principal and interest and premium, if any, represented by the Certificates, and after such payment, the Trust Agreement shall become void.

Deposit of Money or Securities with Trustee. During the Fixed Rate Period and whenever in the Trust Agreement or the Installment Sale Agreement it is provided or permitted that there be deposited with or held in trust by the Trustee Eligible Funds or securities acquired with Eligible Funds in the necessary amount to pay or prepay any Certificates, the Eligible Funds or securities to be so deposited or held may include Eligible Funds or securities held by the Trustee in the funds and accounts established pursuant to the Trust Agreement and shall be:

1. lawful money of the United States of America in an amount equal to the principal amount represented by such Certificates and all unpaid interest represented thereby to maturity, except that, in the case of Certificates which are to be prepaid prior to maturity and in respect of which notice of such prepayment shall have been given or provision satisfactory to the Trustee shall have been made for the giving of such notice, the amount to be deposited or held shall be the principal amount or Prepayment Price and all unpaid interest to such date of prepayment if any, represented by such Certificates; or

2. non-callable, non-prepayable Federal Securities described in clause (a) of the definition thereof which will provide money sufficient to pay the principal at maturity or upon prepayment plus all accrued interest to maturity or to the prepayment date, as the case may be, represented by the Certificates to be paid or prepaid, as such amounts become due, provided that, in the case of Certificates which are to be prepaid prior to the maturity thereof, notice of such prepayment shall have been given or provision satisfactory to the Trustee shall have been made for the giving of such notice;

together with a certificate of an Independent Certified Public Accountant that such amount on deposit, together with interest to accrue thereon and moneys on deposit in the funds and accounts provided for in the Trust Agreement, will be fully sufficient to pay and discharge the obligation to pay the Certificates (including all principal, interest and prepayment premiums) at or before their respective maturity dates, together with an Opinion of Bond Counsel that such deposit will not adversely affect the tax-exempt status of interest on the Certificates; provided, in each case, that the Trustee shall have been irrevocably instructed (by the terms of the Trust Agreement and the Installment Sale Agreement or by Written Request of the District) to apply such money or securities to the payment of such principal or Prepayment Price and interest represented by such Certificates.

Whenever moneys have been deposited with the Trustee pursuant to the Trust Agreement which are insufficient to pay all Outstanding Certificates, the Trustee, at the direction of the District, shall identify the Certificates to be deemed defeased and prepaid at the next Prepayment Date.

Notwithstanding anything in the Trust Agreement to the contrary, in the event that the principal coming due on the Certificates shall be paid by the Bank pursuant to the Facility, the Certificates shall remain Outstanding for all purposes, not be defeased or otherwise satisfied and not be considered paid by the District, and the assignment and pledge of the trust created hereunder and all covenants, agreements and other obligations of the District to the Registered Owners of the Certificates shall continue to exist and shall run to the benefit of the Bank, and the Bank shall be subrogated to the rights of such Registered Owners of the Certificates.

Unclaimed Moneys. Anything contained in the Trust Agreement to the contrary notwithstanding, any moneys held by the Trustee in trust for the payment and discharge of the interest or principal or Prepayment Price represented by any of the Certificates which remain unclaimed for two years after the date of deposit of such moneys if deposited with the Trustee after the date when the interest and principal or Prepayment Price represented by such Certificates have become payable, shall at the Written Request of the District be repaid by the Trustee to the District as its absolute property free from trust, and the Trustee shall thereupon be released and discharged with respect thereto and the Owners shall look only to the District for the payment of the interest and principal or Prepayment Price represented by such Certificates; provided, however, that before being required to make any such payment to the District, the Trustee shall first mail a notice to the Owners of the Certificates so payable, at the address of such Owners as shown on the certificate registration books maintained by the Trustee, that such moneys remain unclaimed and that after a date named in such notice, which date shall not be less than thirty (30) days after the date of the mailing of such notice, the balance of such moneys then unclaimed will be returned to the District.

#### MISCELLANEOUS

Benefits of Trust Agreement Limited to Parties. Nothing in the Trust Agreement expressed or implied is intended or shall be construed to confer upon, or to give or grant to, any person or entity, other than the District, the Trustee, the Bank and the Registered Owners of the Certificates, any right, remedy or claim under or by reason of the Trust Agreement or any covenant, condition or stipulation hereof, and all covenants, stipulations, promises and agreements in the Trust Agreement contained by and on behalf of the District shall be for the sole and exclusive benefit of the District, the Trustee, the Bank and the Registered Owners of the Certificates.

Disqualified Certificates. Certificates owned or held by or for the account to the Corporation or the District (but excluding Certificates held in any pension or retirement fund) shall not be deemed Outstanding for the purpose of any consent or other action or any calculation of Outstanding Certificates provided for in the Trust Agreement, and shall not be entitled to consent to or take any other action provided for in the Trust Agreement.

The Trustee may adopt appropriate regulations to require each Owner of Certificates, before his consent provided for in the Trust Agreement shall be deemed effective, to reveal if the Certificates as to which such consent is given are disqualified as provided in the Trust Agreement.

Waiver of Personal Liability. No director, officer or employee of the District or the Corporation shall be individually or personally liable for the payment of the interest or principal or the prepayment premiums, if any, represented by the Certificates, but nothing contained in the Trust Agreement shall relieve any director, officer or employee of the District or Corporation from the performance of any official duty provided by any applicable provisions of law or by the Installment Sale Agreement or the Trust Agreement.

California Law. The Trust Agreement will be construed and governed in accordance with the laws of the State of California.

## **INSTALLMENT SALE AGREEMENT**

### **ACQUISITION AND CONSTRUCTION OF THE PROJECT; ADDITIONAL COSTS**

Changes to the Project. The District may substitute other improvements for those listed as components of the Project in the Installment Sale Agreement, but only if the District first files with the Corporation and the Trustee a statement of the District:

- (a) identifying the improvements to be substituted and the improvements to the District's facilities they replace in the Project; and
- (b) stating that the estimated costs of construction, acquisition and installation of the substituted improvements are not less than such costs for the improvements previously planned; together with an Opinion of Bond Counsel.

Title. All right, title and interest in each component of the Project (as described in the Installment Sale Agreement) will automatically vest in the District upon completion of such component. Such automatic vesting shall occur without further action by the Corporation, and the Corporation shall, if requested by the District or if necessary to assure such automatic vesting of such interests of title, deliver any and all documents required to assure such vesting.

Additional Costs. After making the Installment Payments, the District shall pay additional costs hereunder ("Additional Costs") any amounts required to be rebated to the United States pursuant to Section 148(f) of the Code in order to maintain the exclusion from gross income of interest represented by the Certificates for purposes of federal income taxation, all costs incurred in connection with the Facility, all amounts due with respect to Bank Certificates, including principal and all accrued and unpaid interest at the Bank Rate, and such amounts in each year as shall be required for the payment of all costs and expenses incurred in connection with the sale to District of the Project, including payment of any fees, costs and expenses in connection with the administration of the Project, payment of all taxes, assessments and governmental charges of any nature whatsoever hereafter levied or imposed by any governmental authority against the Corporation or the Installment Payments and other payments referred to herein, to be made by District (except for income taxes of the Corporation), and payment of all fees, costs and expenses incurred by the Corporation with the prior approval of the District.

## COVENANTS OF DISTRICT

Compliance with Installment Sale Agreement and Ancillary Agreements. The District will punctually pay the Installment Payments and Additional Costs in strict conformity with the terms of the Installment Sale Agreement, and will faithfully observe and perform all the agreements, conditions, covenants and terms contained therein required to be observed and performed by it, and will not terminate the Installment Sale Agreement for any cause including, without limiting the generality of the foregoing, any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Project, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State of California or any political subdivision of either or any failure of the Corporation to observe or perform any agreement, condition, covenant or term contained herein required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected herewith or the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Corporation or any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lock outs, lack of transportation facilities, fire, explosion, or acts or regulations of governmental authorities.

The District will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Trust Agreement required to be observed and performed by it, and it is expressly understood and agreed by and among the parties to the Installment Sale Agreement and the Trust Agreement that each of the agreements, conditions, covenants and terms contained in each such agreement is an essential and material term of the purchase of and payment for the Project by the District pursuant to, and in accordance with, and as authorized under the Law.

Annual Budget. During the Term of the Installment Sale Agreement, the District agrees and covenants to take such action as may be necessary to include all Installment Payments and Additional Costs due under the Installment Sale Agreement in its annual budget and to make the necessary annual appropriations for all such Installment Payments and Additional Costs.

Tax Covenants. The District covenants that, notwithstanding any other provision of the Installment Purchase Agreement, it will make no use of the proceeds of the Certificates or of any other amounts, regardless of the source, or of any property or take no action, or refrain from taking any action, that would cause the Certificates to be "arbitrage bonds" within the meaning of Section 148 of the Code. The District will not use or permit the use of the Project or any portion thereof by any person other than a governmental unit as such term is used in Section 141 of the Code, in such manner or to such extent as would result in the loss of exclusion from gross income for federal income tax purposes of the portion of the Installment Payments constituting interest under Section 103 of the Code. The District will not make any use of the proceeds of the Certificates or any other funds of the District, or take or omit to take any other action, that would cause the obligation provided herein to be "federally guaranteed" within the meaning of Section 149(b) of the Code or "private activity bonds" within the meaning of Section 141 of the Code. To that end, so long as any Installment Payments and Additional Costs are unpaid, the District, with respect to such proceeds and such other funds, will comply with all requirements of such Sections and all regulations of the United States Department of the Treasury issued thereunder and under Section 103 of the Internal Revenue Code of 1954, as amended, to the extent such requirements are, at the time, applicable and in effect.

Collection of Rates and Charges. The District will fix, prescribe and collect rates, fees and charges for the services and commodities provided by the Water System which will be sufficient to yield (i) Taxes and Net Revenues during each Fiscal Year in an amount not less than 120% of the sum of the Installment Payments provided for under the Installment Sale Agreement and on any Parity Debt for such Fiscal Year. On or before the first day of the eighth month of each Fiscal Year, the District will complete a review of its financial condition for the purpose of estimating whether the Taxes and Net Revenues for the then current Fiscal Year will be sufficient to meet the requirements of this section, which review shall be evidenced by a certificate of an Authorized Officer of the District that shall be filed with the Trustee within ten (10) days of

the completion of such review. If such certificate shows that such Taxes and Net Revenues may not be sufficient to meet the requirements of this section, the District will promptly take such action as shall be necessary and sufficient to comply with these requirements, and will promptly advise the Trustee as to such action taken. The District may make adjustments from time to time in such rates, fees and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates, fees and charges then in effect unless the Net Revenues from such reduced rates, fees and charges will at all times be sufficient to meet the requirements of this paragraph.

Rules and Regulations. To the extent permitted by law, the District shall have in effect at all times rules and regulations requiring each consumer or customer located within the service area of the Water System to pay the tolls, rates, fees and charges applicable to the service and commodities provided by the Water System to such premises and providing for the billing thereof and for a due date and a delinquency date for each bill. The District will not permit any part of the Water System, or any facility thereof, to be used or taken advantage of free of charge by any person, firm or corporation, or by any public agency (including the United States of America, the State of California and any public corporation, political subdivision, city, county, district or agency of any thereof); provided, however, that the District may without charge use the services and commodities provided by the Water System. Nothing contained in this paragraph shall prohibit incidental use of Water System facilities by any person, firm, corporation or public agency where such use does not in any manner impair or adversely affect the rights or security of the Certificate Owners.

Insurance. The District shall at all times keep or cause to be kept the properties of the Water System which are of an insurable nature and of the character usually insured by those operating properties similar to the Water System insured against loss or damage by fire and from other causes customarily insured against and in such relative amounts as are usually obtained so long as such insurance is obtainable at reasonable costs. To the extent obtainable at reasonable cost, the District shall at all times use its reasonable efforts to maintain or cause to be maintained insurance or reserves against loss or damage from such hazards and risks to the person and property of others as are usually insured or reserved against by those operating properties similar to the properties of the Water System. To the extent obtainable at reasonable cost, the District shall also use its reasonable efforts to maintain or cause to be maintained any additional or other insurance which it shall deem necessary or advisable to protect its interests and those of the Certificate Owners. Any such insurance shall be in the form of policies or contracts for insurance with insurers of good standing and shall include a loss payable clause making any loss thereunder payable to the Trustee as its interests appear. The District will procure and maintain with responsible insurers workers' compensation insurance against liability for compensation under the Workers Compensation Insurance and Safety Act of California or any act amendatory thereof or supplemental thereto, which insurance shall cover all persons employed in connection with the Water System; provided that such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and manner usually maintained in connection with systems similar to the Water System. Anything in the Installment Sale Agreement to the contrary notwithstanding, the District may be self-insured for all or any part of the foregoing requirements.

Net Proceeds of Insurance. All proceeds of insurance against property damage and all proceeds of condemnation awards relating to the Project shall be payable to the District alone, and the District shall retain and collect such proceeds. All claims under any such insurance policy or with respect to any condemnation proceeding relating to the Project may be settled by the District without the consent of the Corporation or the Trustee. Such proceeds shall be applied promptly to the optional prepayment of Installment Payments, or retained by the District and promptly applied to the repair or rebuilding of the Project or the acquisition or construction of the capital improvements to the Water System.

Payment of Taxes and Assessments; Compliance With Law. The District will from time to time duly pay and discharge, or cause to be paid and discharged, all taxes, assessments and other governmental charges, or required payments in lieu thereof, lawfully imposed upon the properties of the District or upon the rights, revenues, income, receipts, and other moneys, securities and funds of the District, when the same

shall become due (including all rights, moneys and other property transferred, assigned or pledged under the Installment Sale Agreement), and all lawful claims for labor and material and supplies, except those taxes, assessments, charges or claims which the District shall in good faith contest by proper legal proceedings if the District shall in all such cases have set aside on its books reserves deemed adequate with respect thereto. Nothing contained in the Installment Sale Agreement shall require the District to pay any taxes, assessments and other governmental charges which have accrued but are not yet payable, nor shall anything in the Installment Sale Agreement require the District to satisfy any claim or lien for labor, materials or supplies in connection with work performed by for which payment is not yet due.

Financing Statements. The District shall promptly file in accordance with the applicable provisions of the Act and the Uniform Commercial Code in effect in the State of California, all financing statements or similar notices required to fully perfect and continue the perfection of the security interest granted under the Installment Sale Agreement in (i) the proceeds of the sale of the Certificates, (ii) the Taxes and Net Revenue, and (iii) all Funds and Accounts pledged by the Trust Agreement including the investments, if any, thereof. On or before February 1 of each year, the District shall deliver to the Trustee a certificate of an authorized officer of the District to the effect that all filings and other actions then required to continue the perfection of the security interest granted under the Installment Sale Agreement or under the Trust Agreement have been accomplished and setting forth all such filings made and actions taken since the previous such certificate was delivered to the Trustee.

Corporate Existence. The District shall at all times maintain its corporate existence and shall do and perform or cause to be done and performed all acts and things required to be done or performed by or on behalf of the District under the Installment Sale Agreement and the provisions of the Trust Agreement.

Senior Debt. The District shall not incur any obligation payable from the Net Revenues senior to the obligation to make the Installment Payments and shall not sell any portion of the Water System which would impair the ability of the District to make Installment Payments, except that the District may acquire and sell portions of the Water System in the ordinary course of business.

#### PREPAYMENT OF INSTALLMENT PAYMENTS AND DISCHARGE OF OBLIGATIONS

Prepayment. The District shall have the right at any time or from time to time to prepay all or any part of the Installment Payments to the extent that Certificates may be prepaid in accordance with the Trust Agreement, by paying the applicable prepayment price together with accrued interest to the date of prepayment and the Corporation agrees that the Trustee shall accept such prepayments when the same are tendered by the District. Prepayments may be made by payments of Eligible Funds or surrender of Certificates, as contemplated by the Installment Sale Agreement. All such prepayments (and the additional payment of any amount necessary to pay the applicable premiums, if any, payable in Eligible Funds upon the prepayment of Certificates) shall be deposited upon receipt in the Prepayment Account and, at the Request of the District, credited against Installment Payments in order of their due date or used for the prepayment or purchase of Outstanding Certificates in the manner and subject to the terms and conditions set forth in the Trust Agreement. The District shall also have the right to surrender Certificates acquired by it in any manner whatsoever to the Trustee for cancellation, and such Certificates, upon such surrender and cancellation, shall be deemed to be paid and retired, and shall be allocated as set forth in the Trust Agreement. Notwithstanding any such prepayment or surrender of Certificates, as long as any Certificates remain Outstanding, or any Installment Payments or Additional Costs remain unpaid, the District shall not be relieved of its obligations hereunder.

If the District is not in default in the payment of any Additional Costs, the Trustee, at the request of the District, at any time that there is on deposit with the Trustee Eligible Funds or securities acquired with Eligible Funds in the amount necessary to pay or redeem all Certificates Outstanding (as provided in the Trust Agreement), shall forthwith take all steps necessary to discharge and defease the entire indebtedness on all Certificates Outstanding and all covenants, agreements and other obligations of the Corporation or District under the Trust Agreement.

The District also may prepay all or any part of its obligations hereunder and prepay the Certificates pursuant to the Trust Agreement by depositing with the Trustee in the Prepayment Fund Net Proceeds from hazard insurance or condemnation proceeds received with respect to the Water System.

Discharge of Obligations. When:

(a) all Installment Payments shall have become due and payable in accordance with the Installment Sale Agreement or a written notice of the District to prepay all of the Installment Payments shall have been filed with the Corporation; and

(b) during any period the Certificates represent interest calculated at a Fixed Rate there shall have been deposited with the Trustee at or prior to the Installment Payment Dates or date (or dates) specified for prepayment, in trust for the benefit of the Corporation or its assigns and irrevocably appropriated and set aside to the payment of the Installment Payments, sufficient Eligible Funds and/or non-callable, non-prepayable Federal Securities described in clause (a) of the definition thereof acquired with Eligible Funds, the principal of and interest on which when due will provide money sufficient to pay all principal, prepayment premium, if any, and interest of the Installment Payments to their respective Payment Dates or prepayment date or dates as the case may be; and

(c) none of the Installment Payments shall remain unpaid, and provision shall have been made for the payment of all other Additional Costs (including all fees and expenses of the Trustee and the Bank),

then and in that event, the right, title and interest of the Corporation therein and the obligations of the District under the Installment Sale Agreement shall thereupon cease, terminate, become void and be completely discharged and satisfied (except for the right of the Trustee and the obligation of the District to have such moneys and such Federal Securities applied to the payment of the Installment Payments and the covenants of the District as set forth in the Installment Sale Agreement, which shall survive the discharge of the Installment Sale Agreement). In such event, upon request of the District, the Trustee shall cause an accounting for such period or periods as may be requested by the District to be prepared and filed with the District and shall execute and deliver to the District all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee shall pay over to the District, as an overpayment of Installment Payments, all such moneys or such Federal Securities held by it pursuant to the Installment Sale Agreement or pursuant to the Trust Agreement other than such moneys and such Federal Securities as are required for the payment or prepayment of the Installment Payments, which moneys and Federal Securities shall continue to be held by the Trustee in trust for the payment of the Installment Payments and shall be applied by the Trustee to the payment of the Installment Payments of the District.

#### EVENTS OF DEFAULT AND REMEDIES

Events of Default Defined. The following shall be “events of default” under the Installment Sale Agreement and the terms “event of default” and “default” shall mean, whenever they are used in the Installment Sale Agreement, anyone or more of the following events:

(a) Failure by the District to pay any Installment Payment required to be paid under the Installment Sale Agreement at the time set forth therein;

(b) Failure by the District to observe and perform any covenant, condition or agreement on its part to be observed or performed, other than as referred to in the foregoing paragraph (a) for a period of 30 days after written notice by the Corporation, the Trustee, the Bank, if the Facility shall then be in effect, or the Owners of not less than twenty-five percent (25%) in aggregate principal amount of Certificates then Outstanding to the District specifying such failure and requesting that it be remedied; provided, however, if the failure stated in the notice cannot be

corrected within the applicable period, the Corporation, the Trustee, the Bank and such Owners will not unreasonably withhold consent to an extension of such time if corrective action is instituted by the District within the applicable period and diligently pursued until the default is corrected;

(c) Inability of the District to generally pay its debts as such debts become due, or admission by the District, in writing, of its inability to pay its debts generally, or the making by the District of a general assignment for the benefit of creditors, or the institution of any proceeding by or against the District seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding-up, reorganization, reimbursement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or for appointment of a receiver, trustee, or other similar officer of it or any substantial part of its property, or the taking of any action by the District to authorize any of the actions set forth above in this paragraph; and

(d) Any event of default with respect to Parity Debt; and

(e) Receipt by the Trustee of written notice from the Bank of the occurrence of an event of default under the Reimbursement Agreement and electing to exercise remedies available to it under the Reimbursement Agreement, the Trust Agreement and under the Installment Sale Agreement.

Notwithstanding the foregoing provisions, if by reason of force majeure the District is unable in whole or in part to carry out its agreement on its part herein contained, other than the obligations on the part of the District contained in the Installment Sale Agreement, the District shall not be deemed in default during the continuance of such inability. The term "force majeure" as used means, without limitation, the following: acts of God; strikes, lockouts or other industrial disturbances; acts of public enemies; orders or restraints of any kind of the government of the United States of America or of the state wherein the District is located or any of their departments, agencies or officials, or any civil or military authority; insurrections; riots; landslides; earthquakes; fires; storms; droughts; floods; explosions; breakage or accident to machinery; or any other cause or event not reasonably within the control of the District.

**Remedies on Default.** Whenever any event of default referred to in paragraph (a), (c) or (e) above shall have happened and be continuing, the Trustee, as assignee of the Corporation, with the consent of the Bank and subject to the Installment Sale Agreement, shall proceed, or upon occurrence of an event of default specified in paragraph (b) or (d) above, may proceed, and upon written direction of the Bank or written request of the Owners of not less than a majority in aggregate principal amount of then Outstanding Certificates shall proceed to:

(a) declare the entire amount of Installment Payments then outstanding, including the Interest Components thereof then accrued and unpaid, immediately due and payable, without further demand;

(b) take whatever action, at law or in equity, may appear necessary or desirable to collect the Installment Payments and any other payments then due and thereafter to become due under the Installment Sale Agreement or to enforce the performance and observance of any obligation, covenant, agreement or provision contained in the Installment Sale Agreement to be observed or performed by the District; and

(c) take whatever other legal action may appear necessary or desirable to enforce its rights as assignee of the Corporation and the rights of the Owners of the Certificates.

Any such action by the Trustee, however, is subject to the condition that if, at any time after such action and before any judgment or decree for the payment of the moneys due shall have been obtained or entered, there shall be deposited with the Trustee a sum sufficient to pay all Installment Payments the payment of which is overdue, with interest on such overdue principal component of such overdue Installment Payments at the rate borne by the respective Certificates, and the reasonable charges and expenses of the Trustee, and any and all other defaults known to the Trustee (other than in the payment of the Installment Payments due and payable solely by reason of such action) shall have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate shall have been made therefor, then, and in every such case, the Owners of not less than a majority in aggregate principal amount with respect to the Certificates then Outstanding, by written notice to the District and the Trustee may, on behalf of the Owners of all of the Certificates, rescind and annul such action and its consequences and waive such default; but no such rescission and annulment shall extend to or shall affect any subsequent default, or shall impair or exhaust any right or power consequent thereon.

No Remedy Exclusive. No remedy conferred in the Installment Sale Agreement or reserved to the Corporation, the Bank or the Trustee is intended to be exclusive and every such remedy shall be cumulative and shall be in addition to every other remedy given under the Installment Sale Agreement now or hereafter existing at law or in equity. No delay or omission to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver thereof, but any such right and power may be exercised from time to time and as often as may be deemed expedient. In order to entitle the Corporation or the Trustee to exercise any remedy reserved to it in the Installment Sale Agreement it shall not be necessary to give any notice, other than such notice as may be required in the Installment Sale Agreement.

Application of Moneys on Default. In the event of any default under the Installment Sale Agreement, moneys paid shall be applied as provided in the Trust Agreement.

#### AMENDMENTS TO INSTALLMENT SALE AGREEMENT

Amendments, Changes and Modifications. The Installment Sale Agreement and the rights and obligations of the District and the Corporation and of the Owners of the Certificates and of the Trustee may be modified or amended at any time by an amendment thereto which shall become binding when the written consents of the Owners of a majority in aggregate principal amount of the Certificates then Outstanding, exclusive of Certificates disqualified as provided in the Trust Agreement, and the written consent of the Bank shall have been filed with the Trustee. No such modification or amendment shall (1) extend the stated maturities of the Certificates, or reduce the rate of interest represented thereby, or extend the time of payment of interest, or reduce the amount of principal represented thereby, or reduce any premium payable on the prepayment thereof, without the consent of the Owner of each Certificate so affected, or (2) reduce the aforesaid percentage of Owners of Certificates whose consent is required for the execution of any amendment or modification of the Installment Sale Agreement, (3) modify any of the rights or obligations of the Trustee, the Bank or the Corporation without its written consent thereto, or (4) impair the right to tender Certificates pursuant to the Trust Agreement.

The Installment Sale Agreement and the rights and obligations of the District and the Corporation and of the Owners of the Certificates and of the Trustee may also be modified or amended at any time by an amendment thereto which shall become binding upon execution, without the consent of the Owners of any Certificates, but only to the extent permitted by law and only for anyone or more of the following purposes --

- (1) to add to the covenants and agreements of the District or the Corporation contained in the Installment Sale Agreement other covenants and agreements thereafter to be observed or to surrender any right or power herein reserved to or conferred upon the District or the Corporation, and which shall not adversely affect the interests of the Owners of the Certificates;

(2) to cure, correct or supplement any ambiguous or defective provision contained in the Installment Sale Agreement or in regard to questions arising under the Installment Sale Agreement, as the District or the Corporation may deem necessary or desirable and which shall not adversely affect the interests of the Owners of the Certificates;

(3) to make such other amendments or modifications as may be necessary in order to obtain a rating on the Certificates from S&P or any other national rating service; and

(4) with the written consent of the Bank, to make such other amendments or modifications as may be in the best interests of the Owners of the Certificates.

The District shall also obtain an Opinion of Bond Counsel.

Any provision of the Installment Sale Agreement expressly recognizing or granting rights in the Bank may not be amended in any manner which affects the rights of the Bank thereunder without the prior written consent of the Bank.

#### ASSIGNMENT; APPLICABLE LAW

Assignment by Corporation. The Corporation's right, title and interest in, to and under the Installment Sale Agreement, including all Installment Payments and payments of Additional Costs thereunder (except for the Corporation's right to indemnification), are assigned to the Trustee pursuant to the terms of the Trust Agreement concurrently with the execution and delivery of the Installment Sale Agreement. Upon assignment by the Corporation of its rights under the Installment Sale Agreement to the Trustee under the Trust Agreement, the Corporation shall be fully relieved of its obligation to perform any or all of the duties and obligations imposed upon Corporation (except for Corporation's obligations set forth in the Installment Sale Agreement).

Applicable Law. The Installment Sale Agreement shall be governed by and construed in accordance with the laws of the State of California.

**APPENDIX B**  
**DISTRICT AUDITED FINANCIAL STATEMENTS**

## **APPENDIX C**

### **ECONOMIC PROFILE FOR COUNTY OF SAN DIEGO**

#### **Introduction**

The County of San Diego is the southernmost major metropolitan area in the State of California. The County covers 4,255 square miles, extending 70 miles along the Pacific Coast from the Mexican border to Orange County, and inland 75 miles to Imperial County. Riverside and Orange Counties form the northern boundary. The County is approximately the size of the State of Connecticut.

The County is also growing as a major center for culture and education. Over 30 recognized art organizations including the San Diego Opera, the Old Globe Theater productions, the La Jolla Chamber Orchestra, as well as museums and art galleries, are located in the County. Higher education is provided through five two-year colleges and six four-year colleges and universities.

The San Diego Convention Center contains 361,000 square feet of exhibit space and over 100,000 square feet of meeting/banquet rooms. The Convention Center can accommodate events for 30,000-40,000 people.

In addition to the City of San Diego, other principal cities in the County include Carlsbad, Chula Vista, Oceanside, El Cajon, Escondido, La Mesa and National City. Most County residents live within 20 miles of the coast. Farther inland are agricultural areas, principally planted in avocados and tomatoes, while the easternmost portion of the County has a dry, desert-like topography.

## Population

The County has experienced rapid growth and development in the past 15 years. It has become the seventeenth most populous metropolitan area in the United States. The City of San Diego is the eighth most populous city in the United States. Total population for the County is expected to be over 3.63 million by the year 2015.

The following table shows the January 1 State of California Department of Finance estimates of total population in the San Diego region for each year since 2002, and the increase from the previous year.

**TABLE NO. C-1  
COUNTY OF SAN DIEGO AND STATE OF CALIFORNIA  
POPULATION**

Year	COUNTY OF SAN DIEGO		STATE OF CALIFORNIA	
	Population	Percentage Change	Population	Percentage Change
2002	2,920,566		35,063,959	1.7%
2003	2,971,494	1.7%	35,652,700	1.5%
2004	3,010,023	1.3%	36,199,342	1.3%
2005	3,039,424	1.0%	36,676,931	1.1%
2006	3,065,312	0.9%	37,087,005	1.0%
2007	3,096,975	1.0%	37,463,609	1.1%
2008	3,141,700	1.4%	37,871,509	1.0%
2009	3,185,462	1.4%	38,255,508	1.0%
2010	3,224,432	1.2%	38,648,090	1.7%
% Increase Between 2002 - 2010		10.4%		10.2%

Source: State of California, Department of Finance, "E-4 Population Estimates for Cities, Counties and the State, 2001-2010, with 2000 Benchmark."

## Per Capita Income

Per capita income information for the County, the State of California and the United States are summarized in the following table.

**TABLE NO. C-2  
PER CAPITA INCOME  
SAN DIEGO COUNTY, STATE OF CALIFORNIA AND UNITED STATES  
2006 – 2010**

<b>Year</b>	<b>San Diego County</b>	<b>State of California</b>	<b>United States</b>
2006	\$42,801	\$39,358	\$36,629
2007	44,832	41,571	38,615
2008	45,728	43,641	40,208
2009	42,285	(1)	(1)
2010	42,651	43,104	40,584

Source: County of San Diego, Comprehensive Annual Financial Report for the Year Ended June 30, 2010 and State of California Department of Finance; State of California Employment Development Department.

(1) Not Available.

## Employment

**TABLE NO. C-3**  
**COUNTY OF SAN DIEGO, CALIFORNIA, AND UNITED STATES**  
**LABOR FORCE, EMPLOYMENT, AND UNEMPLOYMENT**

Year and Area	Labor Force	Employment	Unemployment	Unemployment Rate
2006				
San Diego	1,499,900	1,440,400	59,400	4.0%
California	17,686,700	16,821,300	865,400	4.9
United States	151,413,000	144,419,000	7,001,000	4.6
2007				
San Diego	1,518,300	1,449,500	68,900	4.5
California	17,928,700	16,970,200	958,500	5.3
United States	153,126,000	146,049,000	7,078,000	4.6
2008				
San Diego	1,547,300	1,455,100	92,300	6.0
California	18,191,000	16,833,400	1,307,600	7.2
United States	154,329,000	145,368,000	8,924,000	5.8
2009				
San Diego	1,552,000	1,402,400	149,600	9.6
California	18,204,200	16,141,500	2,062,700	11.3
United States	154,142,000	139,877,000	14,265,000	9.3
2010				
San Diego	1,557,500	1,393,200	164,300	10.6
California	18,176,200	15,916,300	2,259,900	12.4
United States	(1)	(1)	(1)	(1)

Source: State of California Employment Development Department, Labor Market Information Division and United States Department of Labor, Bureau of Labor Statistics.

(1) Not Available.

The District is located in the San Diego-Carlsbad-San Marcos Metropolitan Statistical Area (MSA). Six major job categories constitute 81.4% of the work force. They are government (18.4%), professional and business services (17.4%), service producing (13.6%), leisure and hospitality (12.5%), educational and health services (12.2%), and manufacturing (7.3%). The March 2011 unemployment rate in the San Diego-Carlsbad-San Marcos MSA was 10.2%. The State of California March 2011 unemployment rate (unadjusted) was 12.3%.

**TABLE NO. C-4**  
**SAN DIEGO-CARLSBAD-SAN MARCOS MSA**  
**WAGE AND SALARY WORKERS BY INDUSTRY <sup>(1)</sup>**  
**(in thousands)**

Industry	2007	2008	2009	2010	2011
Government	225.0	228.7	228.5	227.3	228.9
Other Services	48.2	48.5	47.3	46.7	46.2
Leisure and Hospitality	157.0	161.1	153.1	150.8	155.6
Educational and Health Services	128.7	135.7	144.6	146.8	151.7
Professional and Business Services	221.4	225.2	208.1	203.2	216.1
Financial Activities	81.9	76.6	71.7	67.2	66.9
Information	31.4	31.2	29.9	25.3	25.1
Transportation, Warehousing and Utilities	28.0	29.2	27.3	26.8	27.7
Service Producing					
Retail Trade	146.6	141.7	130.3	127.8	128.7
Wholesale Trade	45.3	45.0	41.4	38.7	40.1
Manufacturing					
Nondurable Goods	25.2	25.1	22.5	21.4	21.7
Durable Goods	77.5	77.9	76.3	71.1	70.1
Goods Producing					
Construction	88.3	77.9	63.9	55.0	54.0
Mining and Logging	<u>0.4</u>	<u>0.4</u>	<u>0.4</u>	<u>0.4</u>	<u>0.4</u>
Total Nonfarm	1,304.9	1,304.2	1,245.3	1,208.5	1,233.2
Farm	<u>10.8</u>	<u>10.9</u>	<u>9.3</u>	<u>9.4</u>	<u>9.6</u>
Total (all industries)	<u>1,315.7</u>	<u>1,315.1</u>	<u>1,254.6</u>	<u>1,217.9</u>	<u>1,242.8</u>

Source: State of California Employment Development Department, Labor Market Information Division, "Industry Employment & Labor Force - by month, March 2010 Benchmark."

<sup>(1)</sup> Annually, as of March.

## Major Employers

The major employers operating within the County as of June 30, 2010 are shown in Table No. C-5.

**TABLE NO. C-5  
COUNTY OF SAN DIEGO  
MAJOR EMPLOYERS**

<b>Employer</b>	<b>Number of Employees</b>	<b>Percent of Total Employment</b>
Federal Government	44,000	3.13%
State of California	42,300	3.00
University of California, San Diego	26,823	1.91
County of San Diego	16,415	1.17
Sharp HealthCare	14,832	1.05
Scripps Health	13,823	0.98
Qualcomm Inc.	11,847	0.84
City of San Diego	10,470	0.74
Kaiser Permanente	7,404	0.53
U.S. Postal Service, San Diego District	6,050	0.43

Source: County of San Diego Comprehensive Annual Financial Report.

## **Transportation**

Excellent surface, sea and air transportation facilities service county residents and businesses. Interstate 5 parallels the coast from Mexico to the Los Angeles area and points north. Interstate 15 runs inland, leading to Riverside-San Bernardino, Las Vegas and Salt Lake City. Interstate 8 runs eastward through the southern United States.

San Diego's International Airport (Lindbergh Field) is located approximately one mile west of the downtown area at the edge of the San Diego Bay. The facilities are owned and maintained by the San Diego Unified Port District and are leased to commercial airlines and other tenants. The airport is the third most active commercial airport in California, served by 18 major airlines. In addition to San Diego International Airport, there are two naval air stations and seven general aviation airports located in the county.

San Diego is the terminus of the Santa Fe Railway's main line from Los Angeles. Amtrak passenger service is available at San Diego with stops at Del Mar and Oceanside in the north county. San Diego's harbor is one of the world's largest natural harbors. The harbor, a busy commercial port, has also become an extremely popular destination for cruise ships. The Port of San Diego is administered by the San Diego Unified Port District, which includes the cities of San Diego, National City, Chula Vista, Imperial Beach and Coronado.

## **Research and Development**

Research and development activity plays an important role in the area's economy. The County is a leading health sciences and biomedical center. Approximately 35,000 persons are engaged in life sciences-related activities in the metropolitan area, with over 28,000 employed directly in health services. In addition to the University of California San Diego campus, other established research institutions in the La Jolla area of the City include the Salk Institute for Biological Studies, the Scripps Clinic and Research Foundation, and the Scripps Institution of Oceanography.

## **Visitor and Convention Activity**

An excellent climate, proximity to Mexico, extensive maritime facilities, and such attractions as the San Diego Zoo and Wild Animal Park, Sea World, Cabrillo National Monument, and Palomar Observatory allow San Diego to attract visitor and convention business each year.

**APPENDIX D**  
**OPINION OF SPECIAL COUNSEL**

## APPENDIX E

### DTC AND THE BOOK-ENTRY-ONLY SYSTEM

*The following description of the Depository Trust Company (“DTC”), the procedures and record keeping with respect to beneficial ownership interests in the Certificates, payment of principal, interest and other payments on the Certificates to DTC Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in the Certificates and other related transactions by and between DTC, the DTC Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the DTC Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters, but should instead confirm the same with DTC or the DTC Participants, as the case may be.*

*Neither the issuer of the Certificates (the “Issuer”) nor the trustee, fiscal agent or paying agent appointed with respect to the Certificates (the “Agent”) take any responsibility for the information contained in this Appendix.*

*No assurances can be given that DTC, DTC Participants or Indirect Participants will distribute to the Beneficial Owners (a) payments of interest, principal or premium, if any, with respect to the Certificates, (b) certificates representing ownership interest in or other confirmation or ownership interest in the Certificates, or (c) redemption or other notices sent to DTC or Cede & Co., its nominee, as the registered owner of the Certificates, or that they will so do on a timely basis, or that DTC, DTC Participants or DTC Indirect Participants will act in the manner described in this Appendix. The current “Rules” applicable to DTC are on file with the Securities and Exchange Commission and the current “Procedures” of DTC to be followed in dealing with DTC Participants are on file with DTC.*

1. The Depository Trust Company (“DTC”), New York, NY, will act as securities depository for the securities (the “Securities”). The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Security certificate will be issued for each issue of the Securities, each in the aggregate principal amount of such issue, and will be deposited with DTC. If, however, the aggregate principal amount of any issue exceeds \$500 million, one certificate will be issued with respect to each \$500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such issue.

2. DTC, the world’s largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect

Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com) and [www.dtc.org](http://www.dtc.org). *The information contained on these Internet sites is not incorporated herein by reference.*

3. Purchases of Securities under the DTC system must be made by or through Direct Participants, which will receive a credit for the Securities on DTC’s records. The ownership interest of each actual purchaser of each Security (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participants’ records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Securities are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Securities, except in the event that use of the book-entry system for the Securities is discontinued.

4. To facilitate subsequent transfers, all Securities deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Securities with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Securities; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Securities are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

5. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Securities may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Securities, such as redemptions, tenders, defaults, and proposed amendments to the Security documents. For example, Beneficial Owners of Securities may wish to ascertain that the nominee holding the Securities for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

6. Redemption notices shall be sent to DTC. If less than all of the Securities within an issue are being redeemed, DTC’s practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

7. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Securities unless authorized by a Direct Participant in accordance with DTC’s MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.’s consenting or voting rights to those Direct Participants to whose accounts Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

8. Redemption proceeds, distributions, and dividend payments on the Securities will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC’s practice is to credit Direct Participants’ accounts upon DTC’s receipt of funds and corresponding detail information from Issuer or Agent, on payable date in accordance with their respective holdings shown on DTC’s records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in

bearer form or registered in “street name,” and will be the responsibility of such Participant and not of DTC, Agent, or Issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of Issuer or Agent, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to Issuer or Agent. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

10. Issuer may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered to DTC.

11. The information in this section concerning DTC and DTC’s book-entry system has been obtained from sources that Issuer believes to be reliable, but Issuer takes no responsibility for the accuracy thereof.

# APPENDIX F

## INFORMATION CONCERNING METROPOLITAN WATER DISTRICT'S WATER SUPPLY

The following information concerning the Metropolitan Water District's water supply is presented as general background data. MWD has entered into certain continuing disclosure agreements pursuant to which MWD is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file certain annual reports, notices of certain material events as defined under Rule 15c2-12 and annual audited financial statements (the "MWD Information") with the Municipal Securities Rulemaking Board which are available online at <http://emma.msrb.org>.

**MWD HAS NOT REVIEWED THIS OFFICIAL STATEMENT AND HAS MADE NO REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO MWD. MWD IS NOT CONTRACTUALLY OBLIGATED, AND HAS NOT UNDERTAKEN, TO UPDATE SUCH MWD INFORMATION, FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE BONDS UNDER RULE 15c2-12.**

MWD faces a number of challenges resulting from a combination of population growth, increased competition for low-cost water supplies, variable weather conditions and increased environmental regulations. MWD's resources and strategies for meeting these long-term challenges are set forth in its Integrated Water Resources Plan, as updated from time to time. See "*Integrated Water Resources Plan ("IRP") and Five-Year Supply Plan*" herein.

It is MWD's declared policy to meet all the supplemental needs of each of its member agencies, including SDCWA. However, MWD's Board adopted a shortage allocation method in February 2008 (the "Water Supply Allocation Plan"). The method allows MWD, in the event of shortages, to allocate water based on uniform reduction by class of water service, with adjustments made for growth, loss of local supply, demand hardening due to implementation of water conservation, and the amount a member agency's dependence on MWD for its total water supply, as well as other water supply related factors. MWD implemented the second stage of the shortage allocation method on July 1, 2009 and began allocating supplies among its member agencies pursuant to the plan. In April 2010, the MWD's Board adopted a resolution recognizing the continuing regional water shortage and again setting the shortage at the second stage of shortfall allocation, which sustained the prior year's regional water reduction of approximately 10%. Due to cool weather in the summer of 2010, impacts of the economic downturn and increased conservation, demand is expected to be less than the shortage allocation for 2010/11. Any extended curtailment could be accompanied by an increase in MWD water charges to its member agencies and consequently could necessitate an increase in water rates to the SDCWA member agencies, including the District.

### MWD Water Supply

MWD's principal sources of water at the Colorado River and the State Water Project ("SWP").

#### Colorado River Water.

Under applicable laws, agreements and treaties governing the use of water from the Colorado River, California is apportioned the use of 4.4 million acre-feet of Colorado River water each year, plus one-half of any surplus that may be available for use collectively in Arizona, California and Nevada as declared on an annual basis by the United States Secretary of the Interior. Under the 1931 priority system that has formed the basis for the distribution of Colorado River water made available to California, MWD holds the fourth priority right of 550,000 acre-feet per year and a fifth priority right of 662,000 acre-feet per

year. MWD's fourth priority right is the last priority within California's basic annual apportionment of 4.4 million acre-feet; however, the fifth priority right is outside of this entitlement and therefore is not considered a firm supply of water. Until 2003, MWD had been able to take full advantage of its fifth priority right as a result of the availability of surplus water and apportioned but unused water. However, Arizona and Nevada have increased their use of water from the Colorado River, significantly reducing unused apportionment available for California since 2002. In addition, a severe drought in the Colorado River Basin reduced storage in system reservoirs, such that MWD stopped taking surplus deliveries in 2003 in an effort to mitigate the effects of the drought. Prior to 2003, MWD could divert over 1.2 million acre-feet in any year, but since that time, MWD's net diversions of Colorado River water have been limited to a low of approximately 633,000 acre-feet in 2006 and a high of approximately 1,105,232 acre-feet in 2009. Average annual net deliveries for 2003 through 2009 were approximately 813,800 acre-feet, with annual volumes dependent primarily on availability of unused higher priority agricultural water and increasing transfers of conserved water. In 2010, MWD's Colorado River Aqueduct deliveries are projected to reach 1.1 million acre-feet for the first time since 2002, including diversions from new programs and transactions under the *Five Year Supply Plan* and the *Quantification Settlement Agreement* ("QSA") described herein.

*Colorado River Aqueduct.* The Colorado River Aqueduct is owned and operated by MWD. Work on the Colorado River Aqueduct commenced in 1933 and water deliveries started in 1941. Additional facilities were completed by 1961 to meet additional requirements of MWD's member agencies. The Colorado River Aqueduct is 242 miles long, starting at Lake Havasu and terminating at Lake Mathews in Riverside County. After deducting for conveyance losses in transporting and storing the water and considering maintenance requirements, up to 1.25 million acre-feet per year may be conveyed through the Colorado River Aqueduct to MWD's member agencies, subject to the availability of Colorado River water.

*California's Colorado River Water Use Plan.* With Arizona's and Nevada's increasing use of their respective apportionments and the uncertainty of continued Colorado River surpluses, in 1997 the Colorado River Board of California, in consultation with MWD, Imperial Irrigation District ("IID"), Coachella Valley Water District ("CVWD"), the Palo Verde Irrigation District ("PVID"), the Los Angeles Department of Water and Power and the San Diego County Water Authority ("SDCWA"), developed a plan for reducing California's use of Colorado River water to its basic annual apportionment of 4.4 million acre-feet when use of that allotment is necessary (the "California Plan"). The May 2000 California Plan proposed to optimize the use of the available Colorado River supply through water conservation, transfers from higher priority agricultural users to MWD's service area and storage programs.

*Quantification Settlement Agreement.* Many of the core elements of the California Plan are being put into effect under the October 2003 Quantification Settlement Agreement (the "QSA") executed by CVWD, IID and MWD. The QSA establishes Colorado River water use limits for IID, CVWD and MWD, provides for specific acquisitions of conserved water and water supply arrangements for up to 75 years, and restores the opportunity for MWD to receive any "special surplus water" under the Interim Surplus Guidelines. See "*Interim Surplus Guidelines*" below. The QSA also allows MWD to enter into other cooperative Colorado River supply programs. Related agreements modify existing conservation and cooperative water supply agreements consistent with the QSA, and set aside several disputes among California's Colorado River water agencies.

Specific programs under the QSA include lining portions of the All-American and Coachella Canals, which are projected to conserve 96,000 acre-feet annually. As a result, 80,000 acre-feet of conserved water is projected to be delivered to SDCWA by exchange with MWD and 16,000 acre-feet is projected to be delivered for the benefit of the La Jolla, Pala, Pauma, Rincon and San Pasqual Bands of Mission Indians, the San Luis Rey Indian Water Authority, the City of Escondido and Vista Irrigation District, by exchange under a water rights settlement annually. An amendment to the IID-MWD 1988 Conservation Agreement and the associated 1989 Approval Agreement extended the term of the 1988 Conservation Agreement and limited the amount of water used by CVWD to 20,000 acre-feet. In 2021, the transfer of

water conserved annually by IID to SDCWA is expected to reach 205,000 acre-feet (see discussion below under the caption "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*"). With full implementation of the programs identified in the QSA, at times when California is limited to its basic apportionment of 4.4 million acre-feet per year, MWD expects to be able to annually divert to its service area approximately 850,000 acre-feet of Colorado River water plus any unused agricultural water that may be available. This is further augmented by the PVID program, which provides up to 129,800 acre-feet of water per year.

A complicating factor in completing the QSA was the fate of the Salton Sea. The Salton Sea is an important habitat for a wide variety of fish-eating birds as a stopover spot along the Pacific flyway. Some of these birds are listed as threatened or endangered species under the State and Federal endangered species acts ("ESAs"). Located at the lowest elevations of an inland basin and fed primarily by agricultural drainage with no outflows other than evaporation, the Salton Sea is trending towards hyper-salinity, which has already impacted the Salton Sea's fishery. This fishery has historically been suitable habitat for the fish-eating birds. The transfer of water from IID to SDCWA, one of the core programs implemented under the QSA, would reduce the volume of agricultural run-off from IID into the Salton Sea, which in turn would accelerate this natural trend of the Salton Sea to hyper-salinity. See "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*" below. The appropriate mitigation for impacts to the Salton Sea from the IID-SDCWA transfer and the larger issue of Salton Sea restoration was addressed by State legislation facilitating implementation of the QSA. In passing that legislation, the Legislature committed the State to undertake restoration of the Salton Sea ecosystem. Restoration of the Salton Sea is subject to selection and approval of an alternative by the Legislature and finding of the associated capital improvements and operating costs. The Secretary for the California Natural Resources Agency submitted an \$8.9-billion preferred alternative for restoration of the Salton Sea to the Legislature in May 2007. While withholding authorization of the preferred alternative, the Legislature has appropriated funds from Proposition 84 to undertake demonstration projects and investigations called for in the Secretary's recommendation. On September 25, 2010 Governor Schwarzenegger signed Senate Bill 51 establishing the "Salton Sea Restoration Council" as a state agency in the National Resources Agency to oversee restoration of the Salton Sea. The newly created Council was directed to evaluate alternative Sale Sea restoration plans, including those evaluated by the Secretary for the National Resources Agency, and to report to the Governor and Legislature by June 30, 2013 with a recommended Salton Sea restoration plan.

The QSA implementing legislation also established the Salton Sea Restoration Fund, which will be funded in part by payments made by the parties to the QSA and fees on certain water transfers among the parties to the QSA. Under the QSA agreements MWD will pay \$20 per acre-foot into the Salton Sea Restoration Fund for any special surplus Colorado River water that MWD elects to take under the Interim Surplus Guidelines. MWD also agreed to acquire up to 1.6 million acre-feet of water conserved by IID, excluding water transferred from IID to SDCWA (see "*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority*" below), if such water can be transferred consistent with plans for Salton Sea restoration, at an acquisition price of \$250 per acre-foot (in 2003 dollars), with net proceeds to be deposited into the Salton Sea Restoration Fund. No conserved water has been made available to MWD under this program. MWD may receive credit for the special surplus water payments against future contributions for the Lower Colorado River Multi-Species Conservation Program (see "*Environmental Considerations*" below). In consideration of these agreements, MWD will not have or incur any liability for restoration of the Salton Sea. As part of an effort to mitigate the effects of the drought in the Colorado River Basin that began in 2000, MWD elected not to take delivery of special surplus Colorado River water that was available from October 2003 through 2004 and from 2006 through 2007. No special surplus water has been available since 2007.

*Sale of Water by the Imperial Irrigation District to San Diego County Water Authority.* On April 29, 1998, SDCWA and IID executed an agreement (the "Transfer Agreement") for SDCWA's purchase from IID of Colorado River water delivered to IID. An amended Transfer Agreement, executed as one of the QSA agreements, set the maximum transfer amount at 205,000 acre-feet in 2021, with the transfer

gradually ramping up to that amount over an approximately twenty-year period, stabilizing at 200,000 acre-feet per year beginning in 2023.

No facilities exist to deliver water directly from IID to SDCWA. Under the Transfer Agreement, conserved water from IID is delivered to SDCWA through existing facilities owned by MWD. MWD and SDCWA entered into an exchange contract that provides for conserved Colorado River water acquired by SDCWA from IID and water conserved from lining the All-American and Coachella Canals to be made available to MWD for diversion at Lake Havasu. By exchange from the sources of water available to MWD, an equal volume of water is delivered to SDCWA through MWD's distribution system. The price payable by SDCWA for these deliveries is calculated using the charges set by MWD's Board from time to time that are applicable to the conveyance of water by MWD on behalf of its member agencies.

*QSA Related Litigation.* On January 28, 2010, MWD was served with a complaint filed by the County of Imperial and the Imperial County Air Pollution Control District alleging that the execution and implementation of the QSA violates the National Environmental Policy Act and federal Clean Air Act. The complaint names the Department of Interior, Secretary of the Interior, Bureau of Reclamation and Commissioner of Reclamation as defendants, and MWD, CVWD, IID and SDCWA as real parties in interest. On March 29, 2010, MWD and the other defendants and real parties filed separate answers to the complaint. On August 23, 2010, MWD and the other real parties intervened as additional defendants. On September 9, 2010 the administrative record was filed with the court. A status conference was scheduled for December 9, 2010, at which time it is anticipated that a briefing schedule would be set. The impact, if any, that the litigation might have on MWD's water supplies cannot be adequately determined at this time.

On November 5, 2003, IID filed a validation action in Imperial County Superior Court, seeking a judicial determination that thirteen agreements associated with the IID/SDCWA water transfer and the QSA are valid, legal and binding. Other lawsuits also were filed challenging the execution, approval and subsequent implementation of the QSA on various grounds. All of the QSA cases were coordinated in Sacramento Superior Court. Between early 2004 and late 2009, a number of pretrial challenges and dispositive motions were filed by the parties and ruled on by the court, which reduced the number of active cases and narrowed the issues for trial, the first phase of which began on November 9, 2009 and concluded on December 2, 2009. One of the key issues in this first phase was the constitutionality of the QSA Joint Powers Agreement, pursuant to which IID, CVWD and SDCWA agreed to commit \$163 million toward certain mitigation and restoration costs associated with implementation of the QSA and related agreements, and the State agreed to be responsible for any costs exceeding this amount. A final judgment was issued on February 11, 2010, in which the court held that the State's commitment was unconditional in nature and, as such, violated the State's debt limitation under the California Constitution. The court also invalidated eleven other agreements, including the QSA, because they were inextricably interrelated with the QSA Joint Powers Agreement. Lastly, the court ruled that all other claims raised by the parties, including CEQA claims related to the QSA Programmatic EIR and the IID Transfer Project EIR, are moot. MWD, IID, CVWD, SDCWA, the State and others have appealed various aspects of the court's ruling, which has been stayed pending outcome of the appeal. If the ruling stands, it could delay the implementation of programs authorized under the QSA or result in increased costs or other adverse impacts. The impact, if any, that the ruling might have on MWD's water supplies cannot be adequately determined at this time.

The Navajo Nation has filed litigation against the Department of the Interior, specifically the Bureau of Reclamation and the Bureau of Indian Affairs, alleging that the Bureau of Reclamation has failed to determine the extent and quantity of the water rights of the Navajo Nation in the Colorado River and that the Bureau of Indian Affairs has failed to otherwise protect the interests of the Navajo Nation. The complaint challenges the adequacy of the environmental review for the Interim Surplus Guidelines (as defined under "*Interim Surplus Guidelines*" below) and seeks to prohibit the Department of the Interior from allocating any "surplus" water until such time as a determination of the rights of the Navajo Nation is completed. MWD has filed a motion to intervene in this action. In October 2004 the court granted the

motions to intervene and stayed the litigation to allow negotiations among the Navajo Nation, federal defendants, CAWCD, State of Arizona and Arizona Department of Water Resources. Recently the Navajo Nation approved the terms of a proposed settlement. Under its terms the Navajo would have specified rights to water from the Colorado River, the Little Colorado River and groundwater basins under the reservation. All Colorado River water would come from Arizona's apportionment. There would be no financial or water resource impact on MWD. The proposed agreement requires approval of all the affected bodies and federal implementing legislation. The litigation stay has been extended until April 13, 2011, to permit the parties to finalize the settlement. In the event the settlement is not finalized, the impact on MWD, if any, cannot be adequately determined at this time.

*Other MWD Colorado River Supply Programs.* MWD has taken steps to enhance its share of Colorado River water through agreements with other agencies that have rights to use such water such as IID, the PVID and the Central Arizona Water Conservation District.

*Interim Surplus Guidelines.* In January 2001, the Secretary of the Interior adopted guidelines (the "Interim Surplus Guidelines") for use through 2016 in determining if there is surplus Colorado River water available for use in California, Arizona and Nevada. The purpose of the Interim Surplus Guidelines is to provide a greater degree of predictability with respect to the availability and quantity of surplus water through 2016. The Interim Surplus Guidelines were later extended through 2026. The Interim Surplus Guidelines contain a series of benchmarks for reductions in agricultural use of Colorado River water within California by set dates.

Under the Interim Surplus Guidelines, MWD initially expected to divert up to 1.25 million acre-feet of Colorado River water annually under foreseeable runoff and reservoir storage scenarios from 2004 through 2016. However, an extended drought in the Colorado River Basin reduced these initial expectations. From 2000 to 2004, snow pack and runoff in the Colorado River Basin were well below average. Although runoff was slightly above average in 2005 and 2008, average annual runoff from 2000 through 2010 was 69% of normal, representing the driest eleven-year period on record. As of November 2010, combined storage in Lake Mead and Lake Powell was at 50 percent of capacity. Lake Mead's elevation had dropped to 1,082 feet above sea level, the lowest elevation since 1937. Lake Powell was at 63 percent of capacity, with 2010 water year runoff above Lake Powell at 72 percent of average.. MWD's initial 2010 diversion approval from the Bureau of Reclamation totaled 935,700 acre-feet plus any unused Priority 1 through 3 water. MWD anticipates its ultimate 2010 diversion approval from the Bureau of Reclamation will be approximately 1.1 million acre-feet.

SNWA and MWD entered into an Agreement Relating to Implementation of Interim Colorado River Surplus Guidelines on May 16, 2002, in which SNWA and MWD agreed to the allocation of unused apportionment as provided in the Interim Surplus Guidelines and on the priority of SNWA for interstate banking of water in Arizona. SNWA and MWD entered into a storage and interstate release agreement on October 21, 2004. Under this program, Nevada can request that MWD store unused Nevada apportionment in California. The amount of water stored through 2009 under this agreement was 70,000 acre-feet. In subsequent years, Nevada may request recovery of this stored water. As part of a recently executed amendment, it is expected that Nevada will not request return of this water until 2022. The stored water provides flexibility to MWD for blending Colorado River water with State Water Project water and improves near-term water supply reliability.

*Lower Basin Shortage Guidelines and Coordinated Management Strategies for Lake Powell and Lake Mead.* In November 2007, the Bureau of Reclamation issued a Final Environmental Impact Statement ("EIS") regarding new federal guidelines concerning the operation of the Colorado River system reservoirs. These new guidelines provide water release criteria from Lake Powell and water storage and water release criteria from Lake Mead during shortage and surplus conditions in the Lower Basin, provide a mechanism for the storage and delivery of conserved system and non-system water in Lake Mead and extend the Interim Surplus Guidelines through 2026. The Secretary of the Interior issued the final guidelines through a Record of Decision signed in December 2007. The Record of Decision and

accompanying agreement among the Colorado River Basin States protect reservoir levels by reducing deliveries during drought periods, encourage agencies to develop conservation programs and allow the states to develop and store new water supplies. The Colorado River Basin Project Act of 1968 insulates California from shortages in all but the most extreme hydrologic conditions.

*Environmental Considerations.* Several fish species and other wildlife species either directly or indirectly have the potential to affect Colorado River operations, thus changing power operations and the amount of water deliveries to the Colorado River Aqueduct. A number of species that are on either “endangered” or “threatened” lists under the federal and/or California ESAs are present in the area of the Lower Colorado River. To address this issue, a broad-based state/federal/tribal private regional partnership, which includes water, hydroelectric power and wildlife management agencies in Arizona, California and Nevada, developed a multi-species conservation plan for the main stem of the Lower Colorado River (the Lower Colorado River Multi-Species Conservation Program or “MSCP”). The MSCP allows MWD to obtain federal and state permits for any incidental take of protected species resulting from current and future water and power operations and to minimize any uncertainty from additional listings of endangered species. The MSCP also covers operations of federal dams and power plants on the Colorado River.

*Seismic Considerations.* MWD’s water conveyance and distribution facilities are designed to either withstand a maximum probable seismic event or to minimize the potential repair time in the event of damage. The five pumping plants on the Colorado River Aqueduct have been buttressed to better withstand seismic events. Other components of the Colorado River Aqueduct are monitored for any necessary rehabilitation and repair. Supplies are dispersed throughout Metropolitan’s service area, and a six-month reserve supply of water normally held in local storage (including emergency storage in Diamond Valley Lake) provides reasonable assurance of continuing water supplies during such events. However, major portions of the California Aqueduct, the Colorado River Aqueduct and MWD’s internal distribution system are located near major earthquake faults, including the San Andreas Fault. A significant earthquake could damage project structures and interrupt the supply of water.

#### State Water Project.

MWD’s other major source of water is the State Water Project (“SWP”). The SWP is owned by the State of California and operated by the California Department of Water Resources (“DWR”). The SWP transports Feather River water stored in and released from Oroville Dam and unregulated flows diverted directly from the San Francisco Bay/Sacramento-San Joaquin Delta Estuary (“Bay-Delta”) south via the California Aqueduct to four delivery points near the northern and eastern boundaries of MWD. The total length of the California Aqueduct is 444 miles.

MWD is one of 29 agencies that have long-term contracts for water service from DWR, and is the largest agency in terms of the number of people it serves (almost 19 million), the share of SWP water to which it has contracted to receive (approximately 46%), and the percentage of total annual payments made to DWR (approximately 58% in 2009). Upon expiration of the State Water Contract term (currently 2035), MWD has the option to continue service under substantially the same terms and conditions. MWD presently intends to exercise this option to at least 2052.

The SWP was originally intended to meet demands of 4.2 million acre-feet per year. Initial SWP facilities were completed in the early 1970’s, and it was envisioned that additional facilities would be constructed as contractor demands increased. Several factors, including public opposition, increased costs, and increased non-SWP demands for limited water supplies, combined to delay the construction of additional facilities. The quantity of SWP water available for delivery each year is controlled by both hydrology and operational considerations. Under a 100% allocation, the State Water Contract provides MWD with 1,911,500 acre-feet of water. Water received from the SWP by MWD over the eight years from 2002 through 2009, including water from water transfer, groundwater banking and exchange programs varied from a low of 908,000 acre-feet in calendar year 2009 to a high of 1,800,000 acre-feet in calendar year 2004. For calendar year 2009, DWR’s allocation to SWP contractors was 40% of contracted amounts,

reflecting low water storage in the State's major reservoirs, below-normal runoff and regulatory restrictions on water exports from the Bay-Delta to protect listed fish species. Under the 40% allocation, MWD received 765,000 acre-feet from its basic allocation, with 908,000 acre-feet of total water delivered from the SWP in 2009, including supplies from water transfers, exchanges and related Five-Year Supply Plan actions delivered through the California Aqueduct.

For calendar year 2010, DWR's initial allocation estimate to SWP contractors was set at five percent of contracted amounts. The estimate was adjusted upwards during the winter and spring and on June 22, 2010, DWR adjusted its allocation to 50 percent of contracted amounts, reflecting late spring storms, a return to normal precipitation and reservoir levels and an above normal Sierra snowpack. For MWD, the revised allocation provides 955,750 acre-feet, or 50 percent of its 1,911,500-acre-foot contractual amount. The allocation is based on SWP yields under pumping restrictions due to the biological opinions for Delta smelt and Chinook salmon. For 2010, MWD projected delivery of 1,160,000 acre-feet to its service area plus approximately 180,000 acre-feet of net deliveries to storage in its Central Valley groundwater storage programs. This includes SWP supplies from water transfers, exchanges and related Five-Year Supply Plan actions delivered through the California Aqueduct.

On December 16, 2010, DWR's initial calendar year 2011 allocation estimate of water from the SWP was increased from 25 percent to 50 percent of SWP contractors' contractual amounts. For MWD, the revised allocation is 955,750 acre-feet, or 50 percent of its 1,911,500 acre-foot contractual amount. This revised 50 percent allocation for 2011, due to fall 2010 storms and improved carryover levels in the state's major reservoirs, is much improved from the previous year's initial five percent allocation and the highest early season water supply outlook in four years. DWR stated that its allocation is a conservative estimate of what DWR expects it can deliver as a percentage of deliveries requested by SWP contractors for 2011. Actual deliveries and revised allocations for 2011 are expected to increase during the year once actual hydrologic and water supply conditions are known.

Due to drought conditions and the court-ordered restrictions described under "*Endangered Species Act Considerations*" below, California Governor Arnold Schwarzenegger issued a proclamation on February 27, 2009 declaring a statewide drought emergency. The proclamation requested that all urban water users in California increase water conservation and directed that various state agencies take action to address impacts of the drought. These actions included expediting approvals for water transfers (provided that such transfers do not injure other legal users of water or unreasonably affect fish and wildlife); pursuing short-term efforts, such as installation of temporary barriers in the Bay-Delta, to protect water quality and water supply; and expediting regulatory consideration of proposed modifications to Bay-Delta water quality standards. Although cold Pacific storms in April and May 2010 significantly improved water supply outlook conditions, as of November 1, 2010, DWR has classified the water year as below normal and the statewide drought emergency was still in effect. [to be updated]*Bay-Delta Regulatory and Planning Activities*. The State Water Resources Control Board ("SWRCB") is the agency responsible for setting water quality standards and administering water rights throughout California. Decisions of SWRCB can affect the availability of water to MWD and other users of SWP water. SWRCB exercises its regulatory authority over the Bay-Delta by means of public proceedings leading to regulations and decisions. These include the Bay Delta Water Quality Control Plan ("WQCP"), which establishes the water quality standards and proposed flow regime of the estuary, and water rights decisions which assign responsibility for implementing the objectives of the WQCP to users throughout the system by adjusting their respective water rights. Since 2000, SWRCB's Water Rights Decision 1641 has governed the SWP's ability to export water from the Bay-Delta for delivery to MWD and other SWP contractors.

The CALFED Bay-Delta Program is a collaborative effort among state and federal agencies to improve water supplies in California and the health of the Bay-Delta watershed. In August 2000, the federal government and the State of California issued a Record of Decision ("ROD") and related documents approving the final programmatic environmental documentation for the CALFED Bay-Delta Program.

Implementing the CALFED Bay-Delta Program has resulted in investment of \$3 billion on a variety of projects and programs to begin addressing the Bay-Delta's water supply, water quality, ecosystem, and levee stability problems. To guide future development of the CALFED Bay-Delta Program and identify a strategy for managing the Bay-Delta as a sustainable resource, Governor Schwarzenegger in September 2006 established, by Executive Order, a Delta Vision process. The Delta Vision process is tied to legislation that created a cabinet-level committee tasked with developing a strategic vision for the Delta. The 41-member Delta Vision Blue Ribbon Task Force issued its Delta Vision Strategic Plan (the "Strategic Plan") on October 17, 2008, providing its recommendations for long-term sustainable management of the Bay-Delta. The Strategic Plan was reviewed by the Delta Vision Committee, chaired by the State Secretary for Resources. The Implementation Report summarizing the Delta Vision Committee's recommendations was submitted to Governor Schwarzenegger on December 31, 2008. These recommendations include completing the BDCP and associated environmental assessments to permit ecosystem revitalization and conveyance water improvements, identifying and reducing stressors to the Bay-Delta ecosystem, strengthening levees, increasing emergency preparedness, continuing funding for the CALFED ecosystem restoration program, updating Bay-Delta regulatory flow and water quality standards to protect beneficial uses of water and working with the State Legislature on a comprehensive water bond package to fund Bay-Delta infrastructure projects.

On November 4, 2009, the State Legislature authorized an \$11.1 billion water bond measure that includes over \$2 billion for Bay-Delta ecosystem restoration, as well as \$3 billion for new water storage and additional funds for water recycling, drought relief, conservation and watershed projects. The bonds are subject to voter approval and were scheduled to be included on the November 2010 ballot; however, in August 2010, the Legislature postponed the bond election to 2012. Related legislation created a new oversight council for the Bay-Delta and directs that the Bay-Delta be managed with the dual goals of water supply reliability and ecosystem protection, sets a statewide conservation target for urban per capita water use of 20% reductions by 2020, provides funding for increase enforcement of illegal water diversions and establishes a statewide groundwater monitoring program.

*Endangered Species Act Considerations.* The listing of several fish species as threatened or endangered under the federal or California Endangered Species Acts (respectively, the "Federal ESA" and the "California ESA" and, collectively, the "ESAs") have adversely impacted SWP operations and limited the flexibility of the SWP. Currently, five species (the winter-run and spring-run Chinook salmon, Delta smelt, North American green sturgeon and Central Valley steelhead) are listed under the ESAs. In addition, on June 25, 2009, the California Fish and Game Commission declared the longfin smelt a threatened species under the California ESA. The United States Fish and Wildlife Service ("USFWS") announced on April 9, 2009, that the Bay-Delta population of longfin smelt does not qualify as a distinct population segment and cannot be listed under the Federal ESA.

The Federal ESA requires that before any federal agency authorizes finds or carries out an action it must consult with the appropriate federal fishery agency to determine whether the action would jeopardize the continued existence of any threatened or endangered species, or adversely modify habitat critical to the species' needs. The result of the consultation is known as a "biological opinion." In the biological opinion the federal fishery agency determines whether the action would cause jeopardy to a threatened or endangered species or adverse modification to critical habitat and recommends reasonable and prudent alternatives or measures that would allow the action to proceed without causing jeopardy or adverse modification. The biological opinion also includes an "incidental take statement." The incidental take statement allows the action to go forward even though it will result in some level of "take," including harming or killing some members of the species, incidental to the agency action, provided that the agency action does not jeopardize the continued existence of any threatened or endangered species and complies with reasonable mitigation and minimization measures recommended by the federal fishery agency.

In 2004 and 2005, the USFWS and National Marine Fisheries Service ("NMFS") issued biological opinions and incidental take statements that govern operations of the SWP and the federal Central Valley Project (the "CVP") with respect to the Delta smelt, the winter-run and spring-run Chinook salmon and

the Central Valley steelhead. In July 2006, the Bureau of Reclamation reinitiated consultation with the USFWS and NMFS with respect to the 2004 and 2005 biological opinions (with the addition of the North American green sturgeon, which was listed in April 2006) following the filing of legal challenges to those biological opinions and incidental take statements described under —*Federal ESA Litigation* below. In a separate action on June 2, 2010, the National Marine Fisheries Service published regulations under the Federal ESA, applying Federal ESA “take” prohibitions to the North American green sturgeon. Existing restrictions on project operations for the benefit of other listed species will also protect the North American green sturgeon and it is unclear whether additional restrictions and impacts on project operations could result from the rule. Under the Federal ESA, critical habitat must also be designated for each listed species. Critical habitat has been designated for each of the currently listed species, including the North American green sturgeon. The NMFS issued critical habitat designation for the North American green sturgeon on October 9, 2009. The habitat designated as critical for the sturgeon includes the lower Feather River, which could have an adverse impact on SWP operations. The extent of any such impacts cannot be determined at this time.

Litigation filed by several environmental interest groups (*NRDC v. Kempthorne*; and *Pacific Coast Federation of Fishermen’s Associations v. Gutierrez*) in the United States District Court for the Eastern District of California alleged that the 2004 and 2005 biological opinions and incidental take statements inadequately analyzed impacts on listed species under the Federal ESA. On May 25, 2007, Federal District Judge Wanger issued a decision on summary judgment in *NRDC v. Kempthorne*, finding the USFWS biological opinion for Delta smelt to be invalid. On December 14, 2007, Judge Wanger issued his Interim Remedial Order and Findings of Fact and Conclusions of Law requiring that the State Water Project and Central Valley Project operate according to certain specified criteria until a new biological opinion for the Delta smelt is issued. Under the Interim Remedial Order, SWP operations were constrained in the winter and spring of 2007/08 by prevailing conditions and the status of the Delta smelt. The USFWS released a new biological opinion on the impacts of the SWP and CVP on Delta smelt on December 15, 2008. MWD, the San Luis & Delta Mendota Water Authority, Westlands Water District, Kern County Water Agency, Coalition for a Sustainable Delta and State Water Contractors, a California nonprofit corporation formed by agencies contracting with DWR for water from the State Water Project (the “State Water Contractors”), the Family Farm Alliance and the Pacific Legal Foundation on behalf of several owners of small farms in California’s Central Valley have filed separate lawsuits in federal district court challenging the biological opinion. MWD’s lawsuit challenging the biological opinion alleges, among other things, that the biological opinion is unlawful and invalid because it failed to use the best available scientific data and information and that the “Reasonable and Prudent Alternative” in the biological opinion, which imposes major water export restrictions, was arbitrary and capricious, and lacked necessary findings. The federal court has consolidated the six lawsuits challenging the Delta smelt biological opinion under the caption *Delta Smelt Consolidated Cases*. The briefings and hearings on motions in these cases and the *Consolidated Salmon Cases* are described below.

On April 16, 2008, in *Pacific Coast Federation of Fishermen’s Associations v. Gutierrez* the court invalidated the 2004 NMFS’s biological opinion for the salmon and other fish species that spawn in rivers flowing into the Bay-Delta. Among other things, the court found that the no jeopardy conclusions in the biological opinion were inconsistent with some of the factual findings in the biological opinion; that the biological opinion failed to adequately address the impacts of SWP and CVP operations on critical habitat and that there was a failure to consider how climate change and global warming might affect the impacts of the projects on salmonid species. The NMFS released its new biological opinion for salmonid species on June 4, 2009. The salmonid species biological opinion contains additional restrictions on SWP and CVP operations. The NMFS calculated that these restrictions will reduce the amount of water the SWP and CVP combined will be able to export from the Bay-Delta by 5 to 7%. DWR estimated a 10% average water loss, expected to begin in 2010, under this biological opinion. See “*State Water Project Operational Constraints*” below for the estimated impact to MWD’s water supply. Six lawsuits have been filed challenging the 2009 salmon biological opinion. These various lawsuits have been brought by the San Luis & Delta Mendota Water Authority, Westlands Water District, Stockton East Water District, Oakdale Irrigation District, Kern County Water Agency, the State Water Contractors and MWD. The

court has consolidated the cases under the caption *Consolidated Salmon Cases*. On May 25, 2010, the court granted the plaintiffs' request for preliminary injunction in the *Consolidated Salmon Cases*, restraining enforcement of two requirements under the salmon biological opinion that limit exported water during the spring months based on San Joaquin River flows into the Bay Delta and reverse flows on the Old and Middle Rivers. On May 27, 2010, the court ruled in the *Delta Smelt Consolidated Cases* that the plaintiffs had established legal and equitable grounds for injunctive relief against enforcement of a similar limitation of reverse flows on the Old and Middle Rivers during the spring months under the Delta smelt biological opinion, but could not enjoin the limitation absent a showing that the Delta smelt are not within imminent risk of entrainment by the projects' pumps. The court deferred issuance of a preliminary injunction while the parties negotiated a compromise for June 2010 project operations. Hearings on motions for summary judgment in the *Delta Smelt Consolidated Cases* were held on July 8 and 9, 2010. On December 14, 2010, Judge Wanger issued a decision on summary judgment in the *Delta Smelt Consolidated Cases* finding that there were major scientific and legal flaws in the Delta smelt biological opinion, and remanding the biological opinion to the USFWS for reconsideration. The court's decision invalidates some of the restrictions on project operations contained in the Delta smelt biological opinion. The court scheduled a hearing on January 4, 2011 to determine what additional steps should be taken in the litigation. [At that time, the court may schedule an interim remedies proceeding to determine how the projects should be operated while the Delta smelt biological opinion is being reconsidered. *update*] Any interim operational restrictions on the projects, and how they may affect MWD's SWP water supply, are unknown. Hearings on motions for summary judgment in the *Consolidated Salmon Cases* commenced on December 16. It is unknown when the court will issue a decision in the *Consolidated Salmon Cases*. On November 13, 2009, the Center for Biological Diversity filed separate lawsuits challenging the USFWS' failure to respond to a petition to change the Delta smelt's federal status from threatened to endangered and the USFWS' denial of federal listing for the longfin smelt. The Delta smelt and longfin smelt cases were filed in the United States District Court for the Eastern and Northern Districts of California, respectively.

*State Water Project Operational Constraints.* DWR has altered the operations of the SWP to accommodate species of fish listed under the ESAs. These changes in project operations have adversely affected SWP deliveries. Restrictions on Bay-Delta pumping under the Interim Remedial Order in *NRDC v. Kempthorne* reduced deliveries of SWP water to MWD by approximately 250,000 acre-feet in 2008 and 199,000 acre-feet in 2009. The impact on total SWP deliveries attributable to the Delta smelt and salmonid species biological opinions combined is estimated to be one million acre-feet in an average year, reducing SWP deliveries from approximately 3.3 million acre-feet to approximately 2.3 million acre-feet for the year under average hydrology. Reductions to SWP total deliveries from the biological opinions are estimated to range from 0.3 million acre-feet during critically dry years to 1.3 million acre-feet in above normal water years. MWD received approximately 908,000 acre-feet of total water deliveries from the SWP in 2009, including its basic allocation and supplies from water transfers, exchanges and related Five-Year Supply Plan actions that will be delivered through the California Aqueduct. The initial allocation to SWP contractors for 2010 was only 5% of their contracted amounts, based on below-average precipitation and regulatory agency restrictions on water exports from the Bay-Delta to protect listed fish species. DWR revisited this allocation as conditions changed, and on June 22, 2010, announced a final allocation of 50% (955,750 acre-feet for MWD). The allocation incorporates anticipated impacts of pumping restrictions due to the biological opinions for Delta smelt and Chinook salmon on SWP yields. On August 24, 2010, DWR reported that approximately 800,000 acre-feet of water was lost from the SWP for calendar year 2010 as a result of pumping restrictions, of which about 370,000 acre-feet would have been made available to MWD.

Operational constraints likely will continue until a long-term solution to the problems in the Bay-Delta is identified and implemented. The Delta Vision process, established by Governor Schwarzenegger, is aimed at identifying long-term solutions to the conflicts in the Bay-Delta, including natural resource, infrastructure, land use and governance issues. In addition, State and federal resource agencies and various environmental and water user entities are currently engaged in the development of the Bay-Delta

Conservation Plan, which is aimed at addressing ecosystem needs and securing long-term operating permits for the SWP.

Other issues, such as the recent decline of some fish populations in the Bay-Delta and surrounding regions and certain operational actions in the Bay-Delta, may significantly reduce MWD's water supply from the Bay-Delta. SWP operational requirements may be further modified under new biological opinions for listed species under the Federal ESA or by the California Department of Fish and Game's issuance of incidental take authorizations under the California ESA. Biological opinions or incidental take authorizations under the Federal ESA and California ESA might further adversely affect SWP and CVP operations. Additionally, new litigation, listings of additional species or new regulatory requirements could further adversely affect SWP operations in the future by requiring additional export reductions, releases of additional water from storage or other operational changes impacting water supply operations. MWD cannot predict the ultimate outcome of any litigation or regulatory process described above, but believed they could have a materially adverse impact on the operation of SWP pumps, MWD's SWP supplies and MWD's water resources.

*Integrated Water Resources Plan ("IRP") and Five-Year Supply Plan.* MWD, its member agencies, sub-agencies and groundwater basin managers developed the IRP that was adopted by the MWD Board in January 1996 as a long-term planning guideline for resources and capital investments. The purpose of the IRP was the development of a preferred resource mix to meet the water supply reliability and water quality needs for the region in a cost effective and environmentally sound manner. This plan was updated in 2004. On October 12, 2010, MWD's Board adopted an IRP update (the "2010 IRP Update") as a strategy to set goals and a framework for water resources development. This strategy enables MWD and its member agencies to manage future challenges and changes in California's water conditions and to balance investments with water reliability benefits. The 2010 IRP Update was formulated with input from member agencies, retail water agencies, and other stakeholders including water and wastewater managers, environmental and business interests and the community. The framework places an emphasis on regional collaboration. The 2010 IRP Update seeks to provide regional flexibility through 2035 by stabilizing MWD's traditional imported water supplies and continuing to develop additional local resources. It also advances long-term planning for potential future contingency resources, such as storm water capture and large-scale seawater desalination, in close coordination with MWD's 26 member agencies and other utilities. The 2010 IRP Update is available on MWD's website. Specific projects that may be developed by MWD in connection with the implementation of the IRP will be subject to future Board consideration and approval, as well as environmental and regulatory documentation and compliance. The information set forth on MWD's web site is not incorporated by reference.

In April 2008, MWD staff began working with MWD's member agencies on a Five-Year Supply Plan to identify specific resource and conservation actions over a five year period, in order to manage water deliveries under continued drought conditions and court-ordered restrictions. The Five-Year Supply Plan focuses on six categories of resource options to improve MWD's reliability from 2010 through 2014. These categories are (1) water conservation, (2) Colorado River transactions, (3) near-term Delta actions, (4) SWP transactions, (5) groundwater recovery, and (6) local resources. The Water Supply Allocation Plan was approved by the MWD Board in February 2008. The Water Supply Allocation Plan provides a formula for equitable distribution of available supplies in case of extreme water shortages within Metropolitan's service area. On April 14, 2009, MWD's Board adopted a resolution declaring a regional water shortage and implementing the Water Supply Allocation Plan, effective July 1, 2009. The Board set the "Regional Shortage Level" at Water Supply Allocation Plan Level 2, which required reduction of regional water use by approximately 10% and resulted in the sale of about 1.89 million acre-feet of MWD water in fiscal year 2009/10. The final 2009/10 allocation for each member agency was dependent upon its local production during the allocation year and determined through a formal local supply certification process with the member agencies. On April 13, 2010, the MWD Board adopted a resolution recognizing the continuing regional water shortage and again setting the Regional Shortage Level at Water Supply Allocation Plan Level 2, which sustains the prior year's regional water use reduction of approximately 10 percent. As of November 2010, the water supply allocation allows for the sale of about 2.12 million acre-

feet of MWD water in fiscal year 2010/11 for municipal and industrial, Interruptible Agricultural Water Program and seawater barrier deliveries. Due to cool weather in summer 2010, impacts of the economic downturn and increased conservation, fiscal year 2010/11 sales are forecasted as of November 2010 to be below the allocated amount of 2.12 million acre-feet of MWD water. The reduced demands allow for additional storage and, if current trends continue, will allow MWD to store approximately 650,000 acre-feet in 2010.

*Additional MWD Water Supply Enhancements.* MWD is currently pursuing voluntary water transfer and storage and exchange programs with the State, federal, public and private water districts and individuals. MWD has entered into groundwater basin storage agreements with the Arvin-Edison Water Storage District and the Semitropic Water Storage District, an agreement with San Bernardino Valley Municipal Water District to coordinate the use of facilities and SWP supplies and groundwater banking and exchange transfer agreements with the Kern Delta Water District and the Mojave Water Agency. MWD has also entered into an agreement with DWR to purchase a portion of the water released by the Yuba County Water Agency, and has been negotiating water purchase, storage and exchange programs with other agencies in the Sacramento and San Joaquin Valleys. MWD also has an exchange transfer and delivery agreement with the CVWD and the Desert Water Agency.

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**FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT**

**by and between**

**OTAY WATER DISTRICT**

**and**

**OTAY SERVICE CORPORATION**

**Dated as of June 1, 2011**

**Relating to**

**OTAY WATER DISTRICT**

**\$15,400,000**

**VARIABLE RATE DEMAND CERTIFICATES OF PARTICIPATION  
(1996 CAPITAL PROJECTS)**

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## FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT

THIS FIRST AMENDMENT TO INSTALLMENT SALE AGREEMENT (the "First Amendment") is dated as of June 1, 2011, by and between the OTAY WATER DISTRICT, a municipal water district organized and existing under the laws of the State of California (the "District"), and the OTAY SERVICE CORPORATION, a nonprofit public benefit corporation existing under the laws of the State of California (the "Corporation"), and amends, in part, the Installment Sale Agreement dated as of June 1, 1996 by and between the District and the Corporation (the "Original Installment Sale Agreement").

### *WITNESSETH:*

WHEREAS, in connection with the execution and delivery of the Original Installment Sale Agreement, the District, the Corporation and The Bank of New York Mellon Trust Company, N.A. (as successor trustee to Chemical Trust Company of California) (the "Trustee") entered into that certain Trust Agreement dated as of June 1, 1996 pursuant to which the Otay Water District Variable Rate Demand Certificates of Participation (1996 Capital Projects) (the "Certificates") were executed and delivered; and

WHEREAS, the existing Facility securing the repayment of the Certificates under the Trust Agreement is expiring and will not be renewed; and

WHEREAS, in accordance with the provisions of Section 5.06 of the Trust Agreement the District desires to cause a Substitute Facility from Union Bank, N.A. to be delivered to the Trustee to replace the existing letter of credit; and

WHEREAS, the expiration of the existing Facility will result in a mandatory tender of the Certificates under the terms of the Trust Agreement on June 3, 2011 (the "Mandatory Tender Date"); and

WHEREAS, the District and the Corporation have determined that the amendments set forth herein are desirable and may be made with the consent of the Bank and the Remarketing Agent, acting in its capacity as the owner of the Certificates on the Mandatory Tender Date ; and

WHEREAS, all acts, conditions and things required by law to exist, to have happened and to have been performed precedent to and in connection with the execution and delivery of this First Amendment do exist, have happened and have been performed in regular and due time, form and manner as required by law, and the parties hereto are now duly authorized to execute and enter into this First Amendment;

NOW, THEREFORE, in consideration of the covenants and provisions herein set forth and for other valuable consideration the receipt and sufficiency of which is hereby acknowledged, the parties hereto do hereby agree as follows:

**Section 1. Amendment of Section 1.01.** Section 1.01 of the Original Installment Sale Agreement is amended, in part, by deleting the defined terms "Custody Agreement," "Information

Services,” “Letter of Credit,” Operation and Maintenance Expenses,” “Remarketing Agreement,” and “Termination Date” and adding the following definitions to Section 1.01 to read as follows:

“Bonds” means all revenue bonds or notes of the District authorized, executed, issued and delivered by the District, the payments of which are on a parity with the Installment Payments and which are secured by a pledge of and lien on the Taxes and Revenues.

“Custody Agreement” means the Custody Agreement dated as of June 1, 2011, between the Custody Agent and the Bank related to Bank Certificates and any similar agreement between the Custody Agent and a Bank providing a Substitute Facility.

“Contracts” means this Installment Sale Agreement and any amendments and supplements hereto, and all contracts of the District authorized and executed by the District, payments under which are on a parity with the Installment Payments and which are secured by a pledge of and lien on the Taxes and Revenues.

“Debt Service” means, for any Fiscal Year, the sum of:

(1) the interest accruing during such Fiscal Year on all outstanding Bonds, assuming that all outstanding serial Bonds are retired as scheduled and that all outstanding term Bonds are prepaid or paid from sinking fund payments as scheduled (except to the extent that such interest is capitalized);

(2) that portion of the principal amount of all outstanding serial Bonds maturing in such Fiscal Year or maturing in the next succeeding Fiscal Year accruing during such Fiscal Year in each case computed as if such principal amounts were deemed to accrue daily during such Fiscal Year in equal amounts;

(3) that portion of the principal amount of all outstanding term Bonds required to be prepaid or paid in such Fiscal Year or during the next succeeding Fiscal Year in each case computed as if such principal amounts were deemed to accrue daily during such Fiscal Year in equal amounts; and

(4) that portion of the installment payments required to be made during such Fiscal Year or during the next succeeding Fiscal Year under all Contracts, in each case computed as if such installment payments were deemed to accrue daily during such Fiscal Year in equal amounts (except to the extent that the interest portion of such installment payments is capitalized);

less the earnings derived from investment of moneys on deposit in any debt service reserve fund, and any construction fund created with respect to any Contracts or Bonds to the extent such earnings are deposited in a debt service fund;

provided that, as to any such Bonds or installment payments due under any Contracts bearing or comprising interest at other than a fixed rate, the rate of interest used to calculate Debt Service shall be one hundred ten percent (110%) of the greater of:

(i) the then current variable interest rate borne by such Bonds or Contracts plus 2%, and

(ii) the highest variable rate borne over the preceding 12 months by outstanding variable rate debt issued by the District or, if no such variable rate debt is at the time outstanding, by variable rate debt of which the interest rate is computed by reference to an index comparable to that to be utilized in determining the interest rate for the debt then proposed to be issued;

provided further that if any series or issue of such Bonds or installment payments due under any Contracts have twenty-five percent (25%) or more of the aggregate principal amount of such series or issue due in any one year, Debt Service shall be determined for the Fiscal Year of determination as if the principal of and interest on such series or issue of such Bonds or installment payments were being paid from the date of incurrence thereof in substantially equal annual amounts over a period of thirty (30) years from the date of calculation; and

provided further that the amount on deposit in a debt service reserve fund on any date of calculation of Debt Service shall be deducted from the amount of principal due at the final maturity of the Bonds and Contracts for which such debt service reserve fund was established and in each preceding year until such amount is exhausted;

provided further that Debt Service shall be reduced by the amount of investment earnings credited to any debt service fund created with respect to Contracts or Bonds; and

provided further that if the Bonds or Contracts constitute Paired Obligations, the interest rate on such Bonds or Contracts shall be the resulting linked rate or the effective fixed interest rate to be paid by the District with respect to such paired obligations.

“Information Services” means the Electronic Municipal Market Access System of the Municipal Securities Rulemaking Board or such other services as are authorized by the Securities and Exchange Commission to receive notices of called bonds as the District may designate in a Written Request of the District delivered to the Trustee.

“Operation and Maintenance Expenses” means (i) costs spent or incurred for maintenance and operation of the Water System calculated in accordance with generally accepted accounting principles, including (among other things) the reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Water System in good repair and working order, and including administrative costs of the District that are charged directly or apportioned to the Water System, including but not limited to salaries and wages of employees, payments to the Public Employees Retirement System, overhead, insurance, taxes (if any), fees of auditors, accountants, attorneys or engineers and insurance premiums, and including all other reasonable and necessary costs of the District or charges (other than debt service payments) required to be paid by it to comply with the terms of the Certificates or of this Agreement or any Contract or of any resolution or indenture authorizing the issuance of any Bonds or of such Bonds; and (ii) costs spent or incurred in the purchase of water for the Water System; but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles or other bookkeeping entries of a similar nature and all capital charges.

“Paired Obligations” means any Bond or Contract (or portion thereof) designated as Paired Obligations in the resolution, indenture or other document authorizing the issuance or

execution and delivery thereof, which are simultaneously issued or executed and delivered (i) the principal of which is of equal amount maturing and to be redeemed or prepaid (or cancelled after acquisition thereof) on the same dates and in the same amounts, and (ii) the interest rates which, taken together, result in an irrevocably fixed interest rate obligation of the District for the term of such Bond or Contract.

“Remarketing Agreement” means the Remarketing Agreement dated as of June 1, 1996, by and between the District and the Remarketing Agent as it may be amended from time to time.

“Termination Date” means the stated expiration date of the Facility as such date may be extended from time to time, or any earlier date on which the Facility then in effect shall terminate, expire or be cancelled.

“Trustee” means The Bank of New York Mellon Trust Company, as successor in interest to Chemical Trust Company of California, or any other bank or trust company which may at any time be substituted in its place pursuant to the terms of the Trust Agreement.

**Section 2. Amendment of Section 4.13.** Section 4.13 of the Original Installment Agreement is deleted in its entirety and amended to read as follows:

Section 4.13. Limitations on Parity Debt Obligations. The District may at any time execute any Contract or issue any Bonds, as the case may be, as Parity Debt, in accordance herewith, provided an Independent Financial Consultant or Certified Public Accountant shall render to and file with the District and the Trustee a written report certifying that Taxes and Net Revenues for any twelve (12) consecutive calendar months in the eighteen (18) calendar months immediately preceding the issuance of the Parity Debt adjusted as set forth below are at least equal to 125% of Debt Service, assuming such additional Contracts had been executed or additional Bonds had been issued at the beginning of such twelve-month period.

For purposes of calculating Net Revenues as set forth in the preceding paragraph, adjustments to the computations of Net Revenues may be made for the following:

(i) any change in service charges which has been adopted subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(ii) customers added to the Water System subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts;

(iii) the estimated change in Net Revenues which will result from the connection of existing residences or businesses to the Water System within one year following completion of any project to be funded or system to be acquired from the proceeds of such additional Bonds or Contracts; and

(iv) the estimated change in Net Revenues which will result from services provided under any long-term, guaranteed contract that extends for the life of the

additional Bonds or Contracts if entered into subsequent to the commencement of the twelve-month period but prior to the date of issuance or execution of the additional Bonds or Contracts.

Notwithstanding the foregoing, Bonds issued or Contracts executed to refund Bonds or Contracts may be delivered without satisfying the conditions set forth above if Debt Service in each Fiscal Year after the Fiscal Year in which such Bonds are issued or Contracts executed is not greater than Debt Service would have been in each such Fiscal Year prior to the issuance of such Bonds or execution of such Contracts.

**Section 3. Amendment of Section 5.01.** Section 5.01(n) of the Original Installment Agreement is deleted in its entirety and Section 5.01(h) and (m) of the Original Installment Agreement are deleted in their entirety and amended to read as follows:

(h) The District will prepare and file with the Trustee and the Bank annually within one hundred eighty (180) days after the close of each Fiscal Year financial statements of the District for the preceding Fiscal Year prepared in accordance with generally accepted accounting principles, together with an Accountant's Report thereon.

(m) The District shall fix, prescribe, revise and collect rates, fees and charges for the services and commodities provided by the Water System which will be at least sufficient to yield during each Fiscal Year Taxes and Net Revenues equal to one hundred twenty-five percent (125%) of the Debt Service for such Fiscal Year. The District may make adjustments from time to time in such rates and charges and may make such classification thereof as it deems necessary, but shall not reduce the rates and charges then in effect unless the Taxes and Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements of this section.

**Section 4. Nature of Amendment.** The District and the Corporation each hereby find and determine that this First Amendment is an amendment made in accordance with Section 12.04(a) of the Original Installment Purchase Agreement which has been consented to by the Remarketing Agent in its capacity as the owner of all outstanding Certificates on the Mandatory Tender Date and with the consent of the Bank.

**Section 5. Effect of Original Installment Sale Agreement.** Except as expressly set forth herein, all provisions of the Original Installment Sale Agreement remain in full force and effect.

**Section 6. Execution in Counterparts.** This First Amendment may be executed in several counterparts, each of which shall be deemed an original, and all of which shall constitute but one and the same instrument.

*[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK.]*

**IN WITNESS WHEREOF**, the parties hereto have executed this Installment Sale Agreement by their officers thereunto duly authorized as of the day and year first written above.

OTAY WATER DISTRICT

By: \_\_\_\_\_  
Its: General Manager

ATTEST:

\_\_\_\_\_  
Secretary of the Board of Directors

OTAY SERVICE CORPORATION

By: \_\_\_\_\_  
Its: Chief Financial Officer

ATTEST:

\_\_\_\_\_  
Secretary of the Board of Directors

ACKNOWLEDGED AND AGREED:

THE BANK OF NEW YORK MELLON TRUST  
COMPANY, N.A., as Trustee

By: \_\_\_\_\_  
Authorized Officer

CONSENTED TO BY:

UNION BANK, N.A.

By: \_\_\_\_\_  
Authorized Officer



STAFF REPORT

TYPE MEETING:	Regular Board Meeting	MEETING DATE:	June 1, 2011
SUBMITTED BY:	Mark Watton, General Manager	W.D./G.P. NO.	DIV. NO.
SUBJECT:	Board of Directors 2011 Calendar of Meetings		

**GENERAL MANAGER'S RECOMMENDATION:**

At the request of the Board, the attached Board of Director's meeting calendar for 2011 is being presented for discussion.

**PURPOSE:**

This staff report is being presented to provide the Board the opportunity to review the 2011 Board of Director's meeting calendars and amend the schedule as needed.

**COMMITTEE ACTION:**

N/A

**ANALYSIS:**

The Board requested that this item be presented at each meeting so they may have an opportunity to review the Board meeting calendar schedule and amend it as needed.

**STRATEGIC GOAL:**

N/A

**FISCAL IMPACT:**

None.

**LEGAL IMPACT:**

None.

General Manager

Attachments: Calendar of Meetings for 2011

**Board of Directors, Workshops  
and Committee Meetings  
2011**

**Regular Board Meetings:**

January 5, 2011  
February 2, 2011  
March 2, 2011  
April 6, 2011  
May 4, 2011  
June 1, 2011  
**July 6, 2011**  
August 10, 2011  
September 7, 2011  
October 5, 2011  
November 2, 2011  
December 7, 2011

**Special Board or Committee Meetings (3<sup>rd</sup>  
Wednesday of Each Month or as Noted)**

January 19, 2011  
February 16, 2011  
March 16, 2011  
April 20, 2011  
May 18, 2011  
**June 15, 2011**  
July 20, 2011  
August 17, 2011  
September 21, 2011  
October 19, 2011  
November 16, 2011  
December 21, 2011

**Board Workshops:**

Budget Workshop: Monday, May 16, 2011

Special Board Meeting/Board Retreat Workshop: TBD



STAFF REPORT

TYPE MEETING:	Regular Board	MEETING DATE:	June 1, 2011
	Daniel Kay <i>Dil</i> Associate Civil Engineer	PROJECT:	Various DIV.NO. ALL
SUBMITTED BY:	Ron Ripperger <i>W</i> Engineering Manager		
APPROVED BY: (Chief)	Rod Posada <i>Rod Posada</i> Chief, Engineering		
APPROVED BY: (Asst GM)	Manny Magaña <i>m magaña</i> Assistant General Manager, Engineering and Operations		
SUBJECT:	Informational Item - Third Quarter Fiscal Year 2011 Capital Improvement Program Report		

GENERAL MANAGER'S RECOMMENDATION:

That the Otay Water District (District) Board of Directors (Board) accepts the Third Quarter Fiscal Year 2011 Capital Improvement Program (CIP) Report for review and receives a summary via PowerPoint presentation.

COMMITTEE ACTION:

Please see Attachment A.

PURPOSE:

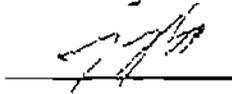
To update the Board about the status of all CIP project expenditures and to highlight significant issues, progress, and milestones on major projects.

ANALYSIS:

To keep up with growth and to meet our ratepayers' expectations to adequately deliver safe, reliable, cost-effective, and quality water, each year the District Staff prepares a six-year CIP Plan that identifies the District infrastructure needs. The CIP is comprised of four categories consisting of backbone capital facilities, replacement/renewal projects, developer's reimbursement projects, and capital purchases.

The Third Quarter Fiscal Year 2011 update is intended to provide a detailed analysis of progress in completing these projects within the allotted time and budget. Expenditures through the Third Quarter totaled approximately \$12.3 million. Approximately 43% of the Fiscal Year 2011 expenditure budget was spent.

FISCAL IMPACT:



None.

STRATEGIC GOAL:

The CIP supports the District's Mission statement, "To provide the best quality of water and wastewater services to the customers of the Otay Water District, in a professional, effective, and efficient manner," and the District's Strategic Goal, in planning for infrastructure and supply to meet current and future potable water demands.

LEGAL IMPACT:

\_\_\_\_\_

None.



General Manager

F:\CIP\CIP Quarterly Reports\2011\Q3\Staff Report\20 06-01-11 Staff Report, Third Quarter FY 2011 CIP Report, (0X-RR-AP).doc  
DK/RR/RP:jf

Attachments: Attachment A - Committee Action  
Presentation



## ATTACHMENT A

SUBJECT/PROJECT: VERLONS	Informational Item - Third Quarter Fiscal Year 2011 Capital Improvement Program Report
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### COMMITTEE ACTION:

Engineering, Operations, and Water Resources Committee reviewed this item at a Committee Meeting held on May 19, 2011 and the following comments were made:

- Staff provided a PowerPoint presentation to the Committee and indicated that expenditures through the Third Quarter totaled approximately \$12.3 million, which is about 43% of the District's Fiscal Year 2011 expenditure budget.
- Staff indicated that the District's FY 2011 CIP budget consists of 82 projects that total \$28.5 million and is divided into four categories:
  - o Capital Facilities= \$16.2 million
  - o Replacement/Renewal= \$10 million
  - o Capital Purchases= \$2.3 million
  - o Developer Reimbursement= \$0 million
- The PowerPoint presentation included the following:
  - o Total Life-to-Date Expenditures thru March 31, 2011
  - o Major CIP Projects
  - o CIP Projects in Construction
  - o Consultant Contract Status of contract amounts, approve payments to date, change orders, dates when contracts were signed and the end date of contracts.
  - o Construction Contract Status thru March 31, 2011 of projects, contract amount, and percent of project completion
  - o Expenditures thru March 31, 2011

Following the discussion, the Committee supported staffs' recommendation and presentation to the full board as an informational item.

# Quality Assurance Approval Sheet

Subject: Informational Item – Third Quarter Fiscal Year  
2011 Capital Improvement Program Report

Project No: Various

Document Description: Staff Report for the June 1, 2011 Board Meeting

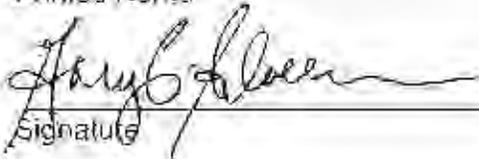
Author:

  
\_\_\_\_\_  
Signature

5/12/11  
\_\_\_\_\_  
Date

Daniel Key  
\_\_\_\_\_  
Printed Name

QA Reviewer:

  
\_\_\_\_\_  
Signature

5/12/11  
\_\_\_\_\_  
Date

Gary Silverman  
\_\_\_\_\_  
Printed Name

Manager:

  
\_\_\_\_\_  
Signature

5/12/11  
\_\_\_\_\_  
Date

Ron Ripperger  
\_\_\_\_\_  
Printed Name

The above signatures attest that the attached document has been reviewed and to the best of their ability the signers verify that it meets the District quality standard by clearly and concisely conveying the intended information; being grammatically correct and free of formatting and typographical errors; accurately presenting calculated values and numerical references; and being internally consistent, legible and uniform in its presentation style.

# CAPITAL IMPROVEMENT PROGRAM



**Third Quarter  
Fiscal Year 2011**  
(through March 31, 2011)

Emergency Interconnections (P2488 & P2489)



1296-1 & 2 Reservoirs Coating (P2490 & P2492)



## Background

The approved CIP budget for Fiscal Year 2011 consists of 82 projects that total \$28.5 million. These projects are broken down into four categories:

- |                             |                 |
|-----------------------------|-----------------|
| 1. Capital Facilities:      | \$ 16.2 million |
| 2. Replacement/Renewal:     | \$ 10.0 million |
| 3. Capital Purchases:       | \$ 2.3 million  |
| 4. Developer Reimbursement: | \$ 0.0 million  |

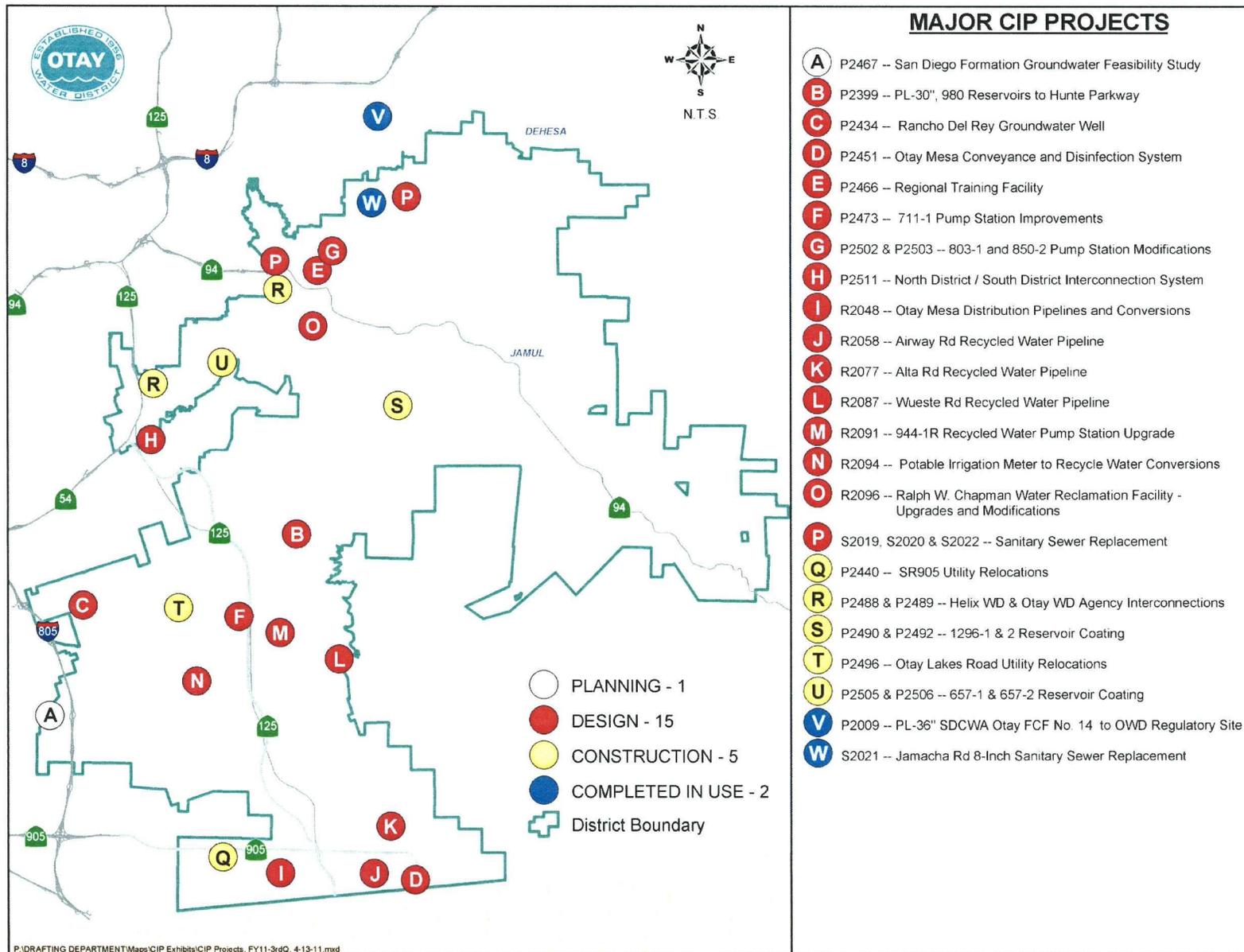
Overall expenditures through the Third Quarter Fiscal Year 2011 totaled \$12.3 million, which is 43% of our fiscal year budget through the third quarter.

# Fiscal Year 2011 Report

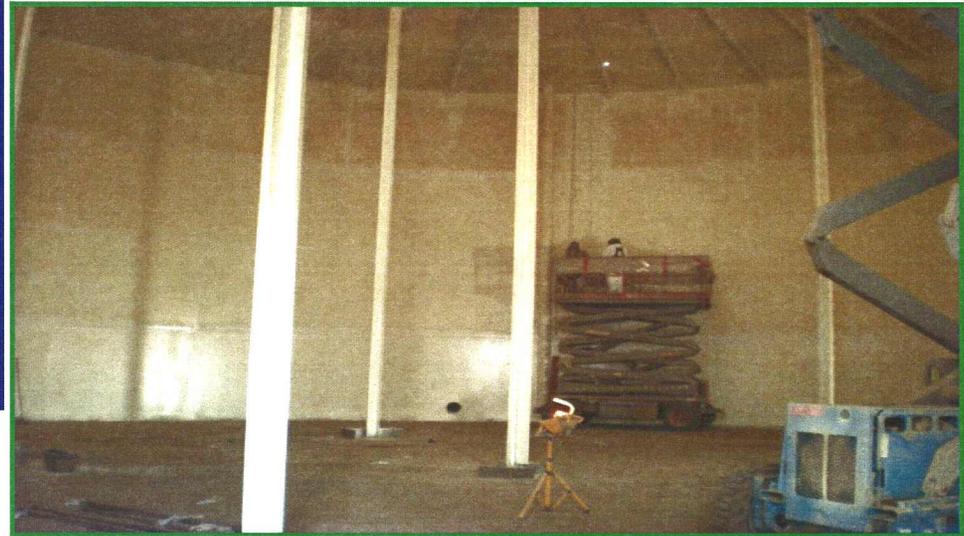
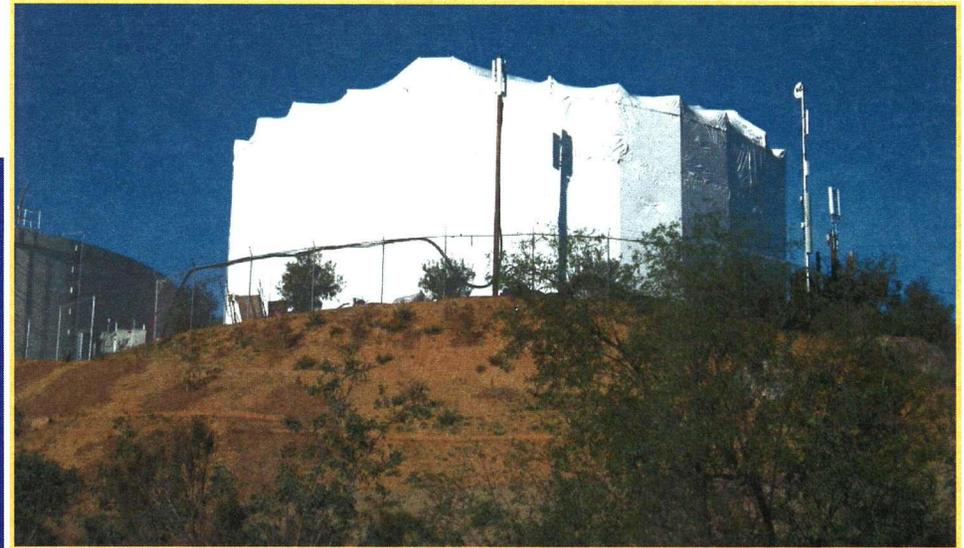
(through March 31, 2011)

CIP CAT	Description	FY 2011 Budget	FY 2011 Expenditures	% FY 2011 Budget Spent	Total Life-to- Date Budget	Total Life-to-Date Expenditures	% Life-to- Date Budget Spent
1	Capital Facilities	\$15,181,000	\$6,703,000	41%	\$180,969,000	\$46,884,000	26%
2	Replacement/ Renewal	\$10,006,000	\$4,410,000	44%	\$44,053,000	\$18,866,000	43%
3	Capital Purchases	\$2,249,000	\$1,160,000	52%	\$11,450,000	\$6,913,000	51%
4	Developer Reimbursement	\$12,000	\$0	0%	\$7,882,000	\$1,000	0%
	Total:	\$28,448,000	\$12,273,000	43%	\$246,354,000	\$72,664,000	29%

# Major CIP Projects



# CIP Projects in Construction



## 1296-1 & 2 Reservoirs Coating (P2490 & P2492)

This project was awarded to West Coast Industrial Coating, Inc. in February 2010. This project includes an assessment of the facilities to assure compliance to all applicable codes and OSHA standards as well as for the interior and exterior coatings of the 1296-1 & 2 Reservoirs.

## CIP Projects in Construction

### □ 1296-1&2 Reservoirs Coating Projects

#### Key

**Component:** Interior and exterior coatings on the 1296-1 & 2 Reservoirs.

**Schedule:** A construction contract was awarded to West Coast Industrial Coating, Inc., on February 3, 2010. Project is approximately 98% complete. Project completion is anticipated for June 2011.

**Cost:** The combined FY 2011 project budgets for CIPs P2490 and P2492 are \$680,000, of which \$705,238, or 104% was spent. The life-to-date project budgets are \$900,000, of which \$916,238, or 102%, have been spent.

#### Significant

**Issues:** The contractor's production has been slower than the submitted schedules. Staff is monitoring the contractor's progress to address the production issues. Due to the extended duration, staff is requesting an increase in the budget for CIP P2490 (1296-1 Reservoir) to accommodate additional costs for this project.

**Highlights:** None.

## CIP Projects in Construction



### 657-1 & 657-2 Reservoir Coating & Upgrades (P2490 & P2492)

This project was awarded to Blastco, Inc. in January 2011.

This project includes an assessment of the facilities to assure compliance to all applicable codes and OSHA standards as well as for the interior and exterior coatings of the 657-1 & 2 Reservoirs.

# CIP Projects in Construction

## □ 657-1 & 2 Reservoirs Coating Projects

### Key

**Component:** Interior and exterior coatings on the 657-1 & 2 Reservoirs.

**Schedule:** A construction contract was awarded to Blastco, Inc., on January 5, 2011. Construction is approximately 37% complete. Project completion is anticipated for July 2011.

**Cost:** The combined FY 2011 project budgets for CIPs P2490 and P2492 are \$650,000, of which \$84,861, or 13% was spent. The life-to-date project budgets are \$750,000, of which \$84,861, or 11%, have been spent.

**Significant  
Issues:** None.

**Highlights:** None.

# CIP Projects in Construction



## Del Rio Road & Gillispie Drive Emergency Interconnections (P2488 & P2489)

This project was awarded to LH Woods & Sons in February 2011.

This project includes two emergency interconnection vaults with Helix Water District.

The work includes a 6-inch meter, vault, and SCADA equipment.

# CIP Projects in Construction

## □ Del Rio Road & Gillispie Drive Emergency Interconnections

### Key

**Component:** Installation of two 6-inch meters, vaults, SCADA, and telemetry equipment for an interconnection with Helix Water District.

**Schedule:** A construction contract was awarded to LH Woods & Sons on February 2, 2011. Construction is approximately 9% complete. Project completion is anticipated for August 2011.

**Cost:** The combined FY 2011 project budgets for CIPs P2488 and P2489 are \$255,000, of which \$66,8691, or 26% was spent. The life-to-date project budgets are \$300,000, of which \$156,689, or 52%, have been spent.

### Significant

**Issues:** None.

**Highlights:** Otay and Helix Water District have an agreement in place to split 50% of the cost for design, construction, and maintenance of the facilities. Otay will receive the reimbursement after construction is complete.

# Consultant Contract Status

(through March 31, 2011)

Consultant	CIP No.	Project Title	Original Contract Amount	Total Change Orders	Revised Contract Amount	Approved Payment To Date	% Change Orders	% Amount Complete
<b>PLANNING</b>								
KECOM	P2434	RANCHO DEL REY GROUNDWATER WELL DEVELOPMENT	\$ 1,581,825.00	\$175,505.00	\$ 1,758,430.00	\$1,719,584.71	11.7%	COMPLETE
MAH AMERICA, INC.	P2010	NORTH SOUTH SERVICES AREA INTERE STUDY	\$ 119,505.00	\$ 11,500.00	\$ 131,005.00	\$ 118,214.41	9.0%	80.0%
SALVADOR O. DRES-CORDOVA	P2451	DESIGNATION PROJECT	\$ 43,000.00	\$ -	\$ 43,000.00	\$ 2,012.94	0.0%	0.0%
TRAM CONSULTING ENGINEERS	07201	SEWERY REVER CCTV INSPECTION AND CONDITION ASSISTANCE	\$ 500,025.00	\$ -	\$ 500,025.00	\$ 254,095.22	0.0%	50.7%
<b>DESIGN</b>								
KECOM	P2451	DTAY MESA CONVEYANCE AND DISINFECTION SYSTEM	\$ 3,910,297.00	\$ -	\$ 3,910,297.00	\$ -	0.0%	0.0%
CALIFORNIA CENTER FOR SUSTAINABLE ENERGY	Varies	SOLAR POWER FEASIBILITY STUDY	\$ 34,400.00	\$ -	\$ 34,400.00	\$ 1,100.00	0.6%	7.9%
CPM PARTNERS	Varies	AS-NEEDED SCHEDULEING SERVICES	\$ 175,000.00	\$ -	\$ 175,000.00	\$ 90,832.50	0.0%	52.0%
DARWELL & ASSOCIATES	Varies	AS-NEEDED TRAFFIC ENGINEERING SERVICES FOR FY2010 AND FY2011	\$ 175,000.00	\$ -	\$ 175,000.00	\$ 141,267.00	0.0%	81.3%
ENGINEERING PARTNERS INC. THE	Varies	ELECTRICAL SERVICES	\$ 100,000.00	\$ -	\$ 100,000.00	\$ 85,000.00	0.0%	85.0%
ENGINEERING PARTNERS INC. THE	Varies	AS-NEEDED ELECTRICAL CONSULTING SERVICES	\$ 100,000.00	\$ -	\$ 100,000.00	\$ 54,320.00	0.0%	54.3%
HRP	Varies	TEMPORARY LABOR SERVICES	\$ 150,000.00	\$ 35,000.00	\$ 185,000.00	\$ 170,800.00	21.3%	92.3%
HVAC ENGINEERING INC.	P2002 P2003	HVAC SERVICES FOR 2001 FT & 600 FT	\$ 19,471.00	\$ -	\$ 19,471.00	\$ 1,075.00	0.0%	5.5%
LEE & NG INC.	P2008	DESIGN OF 36 INCH PPS LINE	\$ 641,812.00	\$ 31,029.00	\$ 641,812.00	\$ 641,812.00	10.0%	COMPLETE
LEE & NG INC.	Varies	AS-NEEDED ENGINEERING DESIGN SERVICES	\$ 175,000.00	\$ -	\$ 175,000.00	\$ 20,862.50	0.0%	11.9%
LEE & NG INC.	P2011	NORTH-SOUTH/SOUTH DISTRICT INTERCONNECTION	\$ 2,758,118.00	\$ -	\$ 2,758,118.00	\$ 220,201.74	0.0%	8.0%
MTSI, INC.	Varies	AS-NEEDED GEOTECHNICAL CONSULTING SERVICES	\$ 175,000.00	\$ -	\$ 175,000.00	\$ 21,460.00	0.0%	12.3%
MICHAEL BAKER CORP.	02010 02001 02002	APPROVAL SERVICES	\$ 17,000.00	\$ -	\$ 17,000.00	\$ 12,050.00	0.0%	70.8%

## Consultant Contract Status (continued)

Consultant	CIP No.	Project Title	Original Contract Amount	Total Change Orders	Revised Contract Amount	Approved Payment To Date	% Change Orders	% Project Complete
<b>DESIGN</b>								
SWH AMERICAS, INC.	R2096, R2095, S2018	RMOWRF UPGRADE PROJECT	\$ 458,813.00	\$122,048.00	\$ 580,861.00	\$ 507,236.09	26.8%	47.3%
ATKINS (via FBS&J)	Varies	HYDRAULIC MODELING SERVICES	\$ 45,000.00	\$ 4,000.00	\$ 49,000.00	\$ 48,987.55	8.9%	COMPLETE
FBS&J	R2517	HYDRAULIC ANALYSIS	\$ 5,000.00	\$ -	\$ 5,000.00	\$ 5,000.00	0.0%	COMPLETE
PHOTO GEODETIC CORPORATION	P2399	SURVEYING SERVICES	\$ 3,425.63	\$ -	\$ 3,425.63	\$ 3,450.00	0.0%	COMPLETE
REPROHALS	Varies	AS-NEEDED REPROGRAPHIC SERVICES	\$ 30,000.00	\$ -	\$ 30,000.00	\$ 7,426.33	0.0%	97.1%
SCHIFF & ASSOCIATES	Varies	PROFESSIONAL CORROSION SERVICES	\$ 250,000.00	\$ 35,000.00	\$ 285,000.00	\$ 222,603.68	14.4%	77.6%
SOUTHERN CALIFORNIA SOIL	Varies	AS-NEEDED GEOTECHNICAL SERVICES	\$ 175,000.00	\$ 11,761.37	\$ 186,761.37	\$ 177,821.83	6.7%	85.2%
S. R. BRADLEY & ASSOCIATES, INC.	P2434	ARCHITECTURAL SERVICES	\$ 5,100.00	\$ -	\$ 5,100.00	\$ 5,100.00	0.0%	COMPLETE
SUPERIOR TANK SOLUTIONS	P2191	803-2 Reservoir Visual Inspection	\$ 250.00	\$ -	\$ 250.00	\$ 250.00	0.0%	COMPLETE
<b>CONSTRUCTION SERVICES</b>								
BRADLEY CONSULTING GROUP	P2172	1485-1 PUMP STATION - TRISE CONSULTING SERVICE	\$ 500.00	\$ -	\$ 500.00	\$ 500.00	0.0%	COMPLETE
MWH CONSTRUCTORS INC.	Varies	TEMPORARY LABOR SERVICES	\$ 150,000.00	\$100,000.00	\$ 250,000.00	\$ 275,100.00	88.7%	COMPLETE
PROWEST APPRAISALS	R0172	APPRAISAL SERVICES	\$ 2,827.50	\$ -	\$ 2,827.50	\$ 2,600.00	0.0%	COMPLETE
RBF CONSULTING	R2069	36-INCH PIPELINE	\$ 1,082,785.00	\$148,070.00	\$ 1,230,855.00	\$1,230,833.75	15.6%	COMPLETE
RBF CONSULTING	R2058, R2077, R2087	CONSTRUCTION MANAGEMENT SERVICES FOR THE OTAY MESA RECYCLED WATER SUPPLY LINK	\$ 708,560.00	\$ -	\$ 708,560.00	\$ 13,960.00	0.0%	2.0%
RBF CONSULTING	S2019 S2021	CONSTRUCTION MANAGEMENT	\$ 5,000.00	\$ -	\$ 5,000.00	\$ 5,000.00	0.0%	COMPLETE
VALLEY CONSTRUCTION MANAGEMENT	Varies	AS-NEEDED CONSTRUCTION MANAGEMENT AND INSPECTION SERVICES	\$ 175,000.00	\$ -	\$ 175,000.00	\$ 105,140.00	0.0%	60.1%

## Consultant Contract Status (continued)

Consultant	CIP No.	Project Title	Original Contract Amount	Total Change Orders	Revised Contract Amount	Approved Payment To Date	% Change Orders	% Project Complete
<b>ENVIRONMENTAL</b>								
A. D. HINSHAW	Values	CONSULTING SERVICES FOR JWA'S CDDA	\$ 34,825.25	\$ -	\$ 34,825.25	\$ 8,500.51	0.0%	24.6%
BRC CONSULTING INC.	P2142	1296-3 RESERVOIR ENV. SVCS	\$ 128,000.00	\$ -	\$ 128,000.00	\$ 134,498.54	0.0%	COMPLETE
FORENSIC ENTOMOLOGY SERVICES	P2454	SCIENCE ADVISOR REVIEW	\$ 4,000.00	\$ -	\$ 4,000.00	\$ 4,000.00	0.0%	COMPLETE
KF INTERNATIONAL (aka JONES & STOKES ASSOCIATES)	P1253	SAN ANGELO HABITAT MANAGEMENT AREA	\$ 987,807.00	\$ -	\$ 987,807.00	\$ 628,018.58	0.0%	63.5%
KF INTERNATIONAL (aka JONES & STOKES ASSOCIATES)	P2058/ P2077/ P2081	DTA'S MESA RECYCLED WATER SUPPLY LINK AND NETC	\$ 213,087.00	\$ 8,115.00	\$ 222,202.00	\$ 222,193.85	4.0%	COMPLETE
KF INTERNATIONAL (aka JONES & STOKES ASSOCIATES)	Values	AD-NEEDC ENVIRONMENTAL CONSULTING SERVICES	\$ 375,000.00	\$ -	\$ 375,000.00	\$ 61,208.19	0.0%	16.3%
DR. MARY ANNE HAYWEE	P2494	SCIENCE ADVISOR REVIEW	\$ 4,380.00	\$ -	\$ 4,380.00	\$ -	0.0%	0.0%
PHOTO DECOFIT CORPORATION	P2096	AERIAL MAPPING	\$ 2,400.00	\$ -	\$ 2,400.00	\$ 2,400.00	0.0%	COMPLETE
PAHN CONSERVATION CONSULTING	P2444	SCIENCE ADVISOR REVIEW	\$ 4,000.00	\$ -	\$ 4,000.00	\$ 4,000.00	0.0%	COMPLETE
RECON	P2451	REVISION OF THE RUBENEA PLAN	\$ 270,853.00	\$ -	\$ 270,853.00	\$ 182,736.39	0.0%	67.5%
TECHNOLOGY ASSOCIATES	P2454	CONSULTING SERVICES FOR JWA'S NDCP	\$ 34,825.25	\$ -	\$ 34,825.25	\$ 33,242.77	0.0%	96.0%
THE RICH ALEXANDER COMPANY (TRAC)	P2494	CONSULTING SERVICES FOR JWA'S NDCP	\$ 30,201.75	\$ -	\$ 30,201.75	\$ 7,388.33	0.0%	24.5%
<b>WATER RESOURCES</b>								
AEDOM	P2481	MIDDLE SANITARY RIVER BASIN GROUNDWATER POLLUTION RISK PROJECT	\$ 1,085,037.00	\$ -	\$ 1,085,037.00	\$ 384,069.69	5.0%	53.0%
CAMP DRESSER & MCKEE INC.	P2461	NATIONAL DESALINATION FEASIBILITY STUDY	\$ 84,552.00	\$ 18,005.00	\$ 112,557.00	\$ 89,577.34	18.0%	87.5%
CITY OF CHULA VISTA	P2382	WASTEWATER TREATMENT FACILITY STUDY	\$ 150,000.00	\$ -	\$ 150,000.00	\$ 109,300.18	0.0%	73.0%
MICHAEL B. WELCH	P2481	ENGINEERING PLANNING SVCS	\$ 40,000.00	\$ -	\$ 40,000.00	\$ 19,440.00	0.0%	48.5%
<b>PUBLIC SERVICES</b>								
ARCIS ENGINEERING MANAGEMENT	Values	RECYCLED WATER PLAN CHECKING, RETROFIT AND INSPECTION SERVICES FOR DEVELOPER PROJECTS	\$ 300,000.00	\$ -	\$ 300,000.00	\$ 171,209.88	0.0%	57.1%
ARCIS ENGINEERING MANAGEMENT	Values	RECYCLED WATER PLAN CHECKING, RETROFIT AND INSPECTION SERVICES FOR DEVELOPER PROJECTS	\$ 300,000.00	\$ -	\$ 300,000.00	\$ 34,528.10	0.0%	11.5%
<b>TOTALS</b>			<b>\$17,789,374.35</b>	<b>\$763,923.37</b>	<b>\$18,553,297.72</b>	<b>\$8,382,790.29</b>	<b>4.3%</b>	

## Construction Contract Status

(through March 31, 2011)

CIP NO.	PROJECT TITLE	CONSTRUCTION CONTRACTOR	ORIGINAL CONTRACT AMOUNT	TOTAL CHANGE ORDERS	REVISED CONTRACT AMOUNT	TOTAL EARNED TO DATE	% OF CHANGE	% PROJECT COMPLETE	EST. COMP. DATE
P2009/ P2038	Jamacha Rd. 36-Inch Pipeline & 12-Inch Pipeline Replacement	CCL Contracting	\$16,189,243	(\$1,781,299)	\$14,407,944	\$14,407,544	-11.00%	100%	September 2010
S2021	Jamacha Rd. 8- Inch Sewer Replacement	A.B. Hashmi	\$91,320	(\$2,226)	\$89,094	\$89,094	-2.44%	100%	September 2010
P2490/ P2492	1296-1 & 1296-2 Reservoir Coating & Upgrades	West Coast Industrial	\$690,000	\$2,580	\$692,580	\$454,690	0.37%	66%	February 2011
P2505/ P2506	657-1 & 657-2 Reservoir Coating & Upgrades	Blastco Inc.	\$632,500	\$0	\$632,500	\$243,010	0.00%	38%	July 2011
P2488/ P2489	Del Rio Road & Gillispie Drive Emergency Interconnections	LH Woods	\$379,000	\$4,981	\$383,981	\$14,000	1.31%	4%	August 2011
<b>TOTALS:</b>			\$17,982,063	(\$1,775,964)	\$16,206,099	\$15,208,738	-9.88%		



# Expenditures (Continued) (\$000)

FUND	Description	Project Manager	FISCAL YEAR TO-DATE 2016/17				LIFE TO-DATE		Comments
			FY 2017 Budget	Expenses	Budget	Expenses to Budget %	Budget	Balance	
<b>CAPITAL FACILITY PROJECTS</b>									
F2488	Off Rd. Road, Hahn and Gray Agency Interconnection	Wes	100	37	63	32%	150	00	Project under construction
F2486	Seismic Upgrade and Dwy Light's Interconnection	Wes	100	49	60	34%	150	74	Project under construction
F2497	West Tower Upgrade Study	Kennedy	150	10	137	7%	250	107	Procuring with RFP's in review
F2502	500.1 Pump Station Modification	Schwann	30	19	11	77%	200	181	RFQ's and A/E's awarded in May 2016. Work awarded in June 2016. HVAC not to start in May 2017.
F2500	500.2 Pump Station Modification	Schwann	150	40	109	23%	500	600	See F2502.
F2510	Associated with Agreements	Kay	25	24	24	96%	270	110	Project on hold
F2511	North District - South District Interconnection System	Schwann	800	1092	606	136%	67,200	26,906	RFQ's underway. Not described 2017.
F2334	Maple - 88th Intersect 4 MO	Kay	200	200	200	100%	2,800	3,775	Project on hold
F2580	Maple - 134th Area Distribution Pipelines Conversion	Kay	250	164	10	65%	2,500	1,874	Design 30% complete
F2058	Maple - 164th 840 Zone - Always Road - Day Reservoir	Kennedy	1,200	160	834	14%	1,500	2,167	Revised budget of \$200k for 2017.
F2077	Maple - 164th 840 Zone - Always Road - Always Road	Kennedy	1,250	136	1,616	2%	4,500	3,864	Revised budget of \$1,300k. Re-statement of requirements exceeds \$1,250k of the budget. Equipment expansion budget for the City of Chula Vista and the City of San Diego. Revised budget to \$300k for 2017.
F2087	Maple - 164th 871 Zone - Maple Road - Day Reservoir	Kennedy	4,200	136	2,340	4%	7,000	6,143	
F2088	Maple - 164th 850 Zone - City Jail - Day Reservoir	Kay	300	6	224	2%	3,500	2,437	Project on hold
F2081	Maple - 164th 1 Pump Station Upgrade 10000 GPM and System Enhancements	W. Porter	1,200	144	1,000	12%	3,000	3,517	Project advanced to bid
F2082	Maple - 164th 1 Reservoir (Lower Level)	Kay	1	163	15	301%	742	1	Project complete
F2003	Maple - 164th 1 Reservoir (Upper Level)	Kennedy	100	127	0	100%	240	26	The City of Chula Vista and City have approved the MBR participation agreement to focus on the required study and design requirements. The City of Chula Vista awarded a consulting contract to BMC to complete the scope of work. A final draft permit has been awarded subcontracting to City and City staff review complete. Permit process is currently under construction and completion of 40% is required.
F2004	Maple - 164th 1 Reservoir (Upper Level)	Kennedy	800	160	140	10%	2,100	1,134	
Total Capital Facility Projects			Total	15,601	2,907	2,422	60,000	34,960	

# Expenditures (Continued) (\$000)

SIF No.	Description	Project Manager	FISCAL YEAR TO DATE 2011				LIFE TO DATE		Comments
			FY 2011 Budget	Expenses	Balance	Percent of Budget %	Budget	Balance	
<b>REPLACEMENT/RENEWAL PROJECTS</b>									
P2369	ARCO Plaza Redooring and Pavement	Goldens	442	134	301	30%	2,203	1,761	Notes that were already to be purchased through FY11 are now covered with FY12.
P2381	Sanity and Security improvements	Manna	100	73	27	73%	1,600	1,527	We are waiting on the private bus stop sign on Camino del Este and this one will be covered in the budget for the 2nd quarter.
P2416	SR 125 Utility Repairs	Wright	50	50	0	100%	323	273	Small projects paying from O&M
P2440	SR28 Utility Repairs	Wright	100	100	0	100%	1,000	1,000	Final amount submitted May 2011
P2450	SR 11 Utility Repairs	Ray	50	1	49	2%	135	134	Contract Award
P2456	Arroyo Valley Water Upgrades	Arroyo	450	441	9	98%	2,177	2,056	Contract
P2466	AMT Solar Water Assessment	Huayan	1,500	1,252	248	83%	10,440	9,188	Expenditures 100% of current fiscal year's budget
P2477	Res. (624) Reservoir Cover Replacement	Wright	5	1	4	20%	450	449	On budget and on schedule
P2484	Water Waste Metal Replacement Program	Huayan	100	115	15	115%	305	290	Expend to use 125% of current fiscal budget
P2485	IT & IT Computer System and Software Replacement	Dicker	750	209	541	28%	1,300	1,091	Final amount submitted May 2011
P2488	AS40 Management Plan Condition Assessment and Data Acquisition	Sowers	600	188	412	31%	1,150	1,062	Project starting outside budget on schedule
P2490	SR 141 Reservoir Interior Slope Coating	Ray	740	317	423	43%	2,500	2,183	Project under construction
P2491	SR 3 Reservoir Exterior Coating	Ray	10	1	9	10%	200	199	Project in the month of FY12
P2497	SR 2 Reservoir Interior Slope Coating	Ray	440	396	44	90%	390	390	Project under construction
P2498	SR 2 Reservoir Exterior Coating	Ray	5	5	0	100%	80	80	Project in the month of FY12
P2494	Multiple Sources Contamination Plan	Erwin-Royce	100	164	114	164%	600	108	The budget will be spent this fiscal year
P2495	Tan Miguel Highway Maintenance/Mileage Plan	Cooper-Royce	250	150	100	60%	1,175	1,025	This budget will be spent this fiscal year
P2496	Day Care Road Utility Relocations	Ray	180	16	164	9%	250	234	Phase 1 Construction complete
P2504	Regulatory Soil Access Road and Pipeline Relocation	Sowers	200	7	193	4%	600	593	Construction
P2505	SR 7-1 Reservoir Interior Slope Coating	Cooper	325	124	201	38%	315	251	In construction
P2506	SR 7-1 Reservoir Exterior Slope Coating	Cooper	125	30	95	24%	175	145	In construction
P2507	East Highway Storm Water Diversion	Cooper	30	16	14	53%	100	84	Construction
P2508	Spokane Catholic Protestant Replacement Program	Reynolds	50	50	0	100%	150	150	Project budget to spend for FY11
P2509	R. J. Crockett Public Water Meter Upgrade	Wright	0	0	0	0%	50	50	No progress for Q3
P2606	DMV/DMV Upgrade and Modifications	Cooper-Royce	1,200	564	636	47%	2,500	1,936	The project budget will be spent by the end of the projected budgeted for spend this fiscal year.
P2613	SR 302 Sewer and Road Replacement and DM Relocation	Plankly	643	1	642	0%	4,380	3,738	Final year
P2618	Avocado Boulevard B-Walk Sewer Main Relocation	Cooper	1,215	134	1,081	9%	1,750	1,616	Design complete, preparing for construction
P2620	Salinas Drive B-Walk Sewer Main Relocation	Cooper	80	11	69	14%	470	174	Design complete, preparing for construction
P2621	Armadillo Road B-Walk Sewer Main Relocation	Ray	40	100	60	273%	180	180	Project complete
P2622	Hodden Mesa Drive B-Walk Sewer Main Relocation	Cooper	120	7	113	6%	180	171	Design complete, preparing for construction
P2623	Dicker Drive Sewer Main Utility Relocation	Cooper	30	5	25	16%	80	75	Construction
P2624	Upperville Drive Sewer Main Relocation	Cooper	10	2	8	20%	100	98	Construction
P2625	Wichita Way Sewer Main Relocation	Cooper	10	4	6	40%	175	161	Construction
Total Replacement/Renewal Projects			10,000	4,890	5,110	49%	44,240	39,351	

