$4,300,000,000
STATE OF CALIFORNIA
DEPARTMENT OF WATER RESOURCES
INTERIM ENERGY FINANCING BRIDGE LOAN

TRANSCRIPT INDEX

Tab No.	Document Description
A.	**AUTHORIZATION OF LOANS AND BONDS**
1.	Credit and Security Agreement, dated June 26, 2001, by and between the Department of Water Resources and the Lenders identified therein
2.	Executive Order D-42-01, dated June 18, 2001 of the Governor of the State of California
3.	Emergency Proclamation dated January 17, 2001
4.	DWR Determination to issue Bonds, including certification of mechanisms to ensure timely repayment of Bonds [CSA 4.1(b)(i) and 4.1(g)]*
5.	Treasurer approval of issuance of Bonds [CSA 4.1(b)(ii)]
6.	Director of Finance approval of issuance of Bonds and notification to chairpersons of Joint Legislative Budget Committee and Senate and Assembly committees responsible for appropriations [CSA 4.1(b)(iii)]
B.	**LEGISLATIVE AND REGULATORY PROCEEDINGS**
7.	Certified copies of Assembly Bill 1 of the 1st Extraordinary Session of 2001 (Chapter 4 of the Statutes of 2001 1st Extraordinary Session) (AB1X) and Senate Bill 31 of the 1st Extraordinary Session of 2001 (Chapter 9 of the Statutes of 2001 1st Extraordinary Session)

* CSA references are to the Credit and Security Agreement.

8. Certified copies of Decision No. 01-03-009 dated March 7, 2001, issued by CPUC on March 9, 2001, relating to revenue requirements [CSA 4.1(k)], and Decision No. 01-04-003 dated and issued by CPUC on April 3, 2001

9. Certified copy of Decision No. 01-03-081 dated March 27, 2001, issued by CPUC on March 29, 2001, relating to California Procurement Adjustment, segregation and collection of revenues, and other matters

10. Certified copies of Decision No. 01-04-005 dated April 3, 2001, issued by CPUC on April 4, 2001, relating to California Procurement Adjustment, and Decision No. 01-05-063 dated May 14, 2001, issued by CPUC on May 16, 2001, denying rehearing of Decision No. 01-04-005

11. Acceptance by DWR of D.01-04-005

12. Certificate of CPUC relating to CPUC decisions and DWR acceptance [CSA 4.1(k)]

C. CERTAIN OTHER REQUIREMENTS OF CREDIT AND SECURITY AGREEMENT

13. Taxable Bond issued to each Lender with a taxable loan commitment [CSA 4.1(a)]

14. Tax-Exempt Bond issued to each Lender with a tax-exempt loan commitment [CSA 4.1(a)]

15. Indicative rating letters from Moody's, S&P and Fitch relating to $6 billion of bonds [CSA 4.1(h)]

16. Tax Certificate, including (i) Certificate of Lead Arranger as to issue price and related matters, and (ii) Form 8038-G [CSA 4.1(i)]

17. Certificate of DWR as to no Material Adverse Effect [CSA 4.1(j)]

18. Syndication Agreement

19. Evidence of payment of fees [CSA 3.1(a), (b) and (d) and 4.1(m)]

D. OTHER CONDITIONS PRECEDENT TO ISSUANCE OF BONDS

20. DWR Incumbency and Signature Certificate

21. DWR and Treasurer Receipt for Loan Proceeds

22. Agent's Receipt for Loan Proceeds in Interest and Fees Account

23. Certificate of DWR as to Power Supply Agreements, with redacted copies of Power Supply Agreements

E. OPINIONS

24. Litigation Certificate of Attorney General [CSA 4.1(c)]

25. Approving Opinion of Attorney General [CSA 4.1(c)]

26. "Jarvis" opinion of Attorney General [CSA 4.1(c)]

27. "Hendricks" opinion of Attorney General [CSA 4.1(c)]

28. Opinion of Chief Counsel of DWR [CSA 4.1(d)]

29. Opinion of Special Counsel to DWR [CSA 4.1(e)]

✓ 30. Opinion of Bond Counsel [CSA 4.1(f)]

✓ 31. "Jarvis" opinion of Bond Counsel

✓ 32. Bankruptcy opinion of Bond Counsel

33. Bankruptcy opinion of Special Counsel to DWR

✓ 34. Bond Counsel Opinion Addressed to TO Issuer

35. Reliance Opinion of Bond Counsel to Lehman Custodian

F. MISCELLANEOUS DOCUMENTS

36. Certificate of DWR relating to historical activities and scope of duties

37 Certified copy of Initial DWR Revenue Requirement Communicated to CPUC

38. Letters from DWR and the Department of Finance to the Attorney General Concerning Issuance of the Executive Order

39. Proposed and Final Notices filed with CDIAC

[EXECUTION COPY]

CREDIT AND SECURITY AGREEMENT

among

THE STATE OF CALIFORNIA
acting through the
DEPARTMENT OF WATER RESOURCES,

VARIOUS LENDERS,

and

MORGAN GUARANTY TRUST COMPANY OF NEW YORK,
as Agent

Dated as of June 26, 2001

Lead Arranger and Book Manager
J.P. MORGAN SECURITIES INC.

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EXHIBIT F	FORM OF JOINDER

This CREDIT AND SECURITY AGREEMENT dated as of June 26, 2001 is entered into among THE STATE OF CALIFORNIA acting through the DEPARTMENT OF WATER RESOURCES (the "Department"), the financial institutions from time to time party to this Agreement, each a "Lender" and collectively, the "Lenders"), and MORGAN GUARANTY TRUST COMPANY OF NEW YORK, acting in the manner and to the extent described in Section 8 (in such capacity, together with any successor appointed hereunder, or successor by means of merger, the "Agent").

WITNESSETH:

WHEREAS, subject to and upon the terms and conditions herein set forth, the Lenders are willing to make available to the Department the credit facility provided for herein;

NOW, THEREFORE, IT IS AGREED:

SECTION 1. DEFINITIONS AND PRINCIPLES OF CONSTRUCTION.

1.1. 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):

"AB1X" shall mean Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, as in effect on the date hereof and, from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session as approved by the Governor on May 10, 2001 and filed with the California Secretary of State on May 10, 2001, as in effect on the date hereof.

"Additional Commitment" shall have the meaning provided in Section 2.1(c).

"Additional Lender" shall have the meaning provided in Section 2.1(c).

"Additional Taxable Commitment" shall have the meaning provided in Section 2.1(c).

"Additional Tax-Exempt Commitment" shall have the meaning provided in Section 2.1(c).

"Additional Tax-Exempt Purposes" shall have the meaning provided in Section 9.19.

"Additional Taxes" shall have the meaning provided in Section 3.6.

"Adjusted LIBOR" shall mean, with respect to each Interest Period for a LIBOR Loan, the rate per annum (rounded upward if necessary to the nearest one-sixteenth of one percent) equal to (a) the LIBOR for such Interest Period divided by (b) 1.00 minus the Reserve Requirement Rate (expressed as a decimal fraction) for such Interest Period.

"Affiliate" shall mean, with respect to any Person, any other Person (other than an individual) directly or indirectly Controlling, Controlled by, or under direct or indirect common Control with, such Person.

"Agent" shall have the meaning provided in the first paragraph of this Agreement.

"Agent-Related Person" shall mean Morgan Guaranty Trust Company of New York and any successor Agent under Section 8.9, together with their respective Affiliates (including, in the case of Morgan Guaranty Trust Company of New York, the Lead Arranger) and the officers, directors, employees, agents and attorneys-in-fact of such Persons and Affiliates.

"Agreement" shall mean this Credit and Security Agreement, as modified, supplemented, restated, replaced or amended from time to time.

"Applicable Margin" shall mean, with respect to any Base Rate Loan and, from and after the Term Out First Period, any Tax-Exempt Loan, the applicable margin set forth below opposite the Applicable Period:

Applicable Period	Base Rate Loans	Tax-Exempt Loans
Initial Period	0.00%	N/A
Term Out First Period	0.00%	0.00%
Term Out Second Period	1.00%	1.00%
Term Out Final Period	2.00%	2.00%

"Applicable Period" shall mean the Initial Period, the Term Out First Period, the Term Out Second Period or the Term Out Final Period.

"Assignee" shall mean any Person to whom all, or any ratable part of all, of the Loans and the other rights and obligations of a Lender under the Credit Documents shall be assigned in accordance with Section 9.4.

"Assignment and Acceptance Agreement" shall have the meaning set forth in Section 9.4(d).

"Authorized Representative" shall mean the Director of Water Resources, any Deputy Director of the Department, the Chief, Division of Fiscal Services of the Department, the Deputy Controller of the Department or any other officer of the Department designated to serve as "Authorized Representative" in accordance with Section 1.2(m).

"Base Rate" shall mean, as of any date of determination, the rate determined by the Agent to be the higher of (a) the Prime Rate on that date and (b) the aggregate of the Federal Funds Rate on that date plus 0.50%.

"Base Rate Loan" shall mean any Loan or portion thereof, the interest on which is calculated by reference to the Base Rate.

"Bond" shall mean, as the context requires, a Taxable Bond, a Tax-Exempt Bond or both.

"Business Day" shall mean (a) for all purposes other than as covered by clause (b) below, any day except Saturday, Sunday and any day which shall be in New York, New York or

Sacramento, California a legal holiday or a day on which banking institutions are authorized or required by law or other government action to close and (b) with respect to all notices and determinations in connection with, and payments of principal and interest on, LIBOR Loans, any day which is a Business Day described in clause (a) above and which is also a day for trading by and between banks in the London interbank Eurodollar market.

"Capitalized Interest and Fees Amount" shall mean, at the time any Loans are made, 4.5% of the aggregate principal amount of such Loans.

"Change in Law" shall mean (a) the adoption after the date hereof of a law, regulation, rule or order or directive of a Governmental Authority and/or (b) the amendment, modification or repeal of a law, regulation, rule or order or directive of a Governmental Authority after the date hereof.

"Closing Date" shall mean the first date on which all of the conditions precedent specified in Section 4.1 have been satisfied or waived by the Agent and the Initial Lenders.

"Code" shall mean the Internal Revenue Code of 1986.

"Collateral" shall mean the Interest and Fees Account, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith.

"Commitment" shall mean for each (a) Initial Lender, its Taxable Commitment, its Tax-Exempt Commitment or both and (b) Additional Lender, its Additional Taxable Commitment, its Additional Tax-Exempt Commitment or both.

"Contingent Obligation" shall mean any obligation of the Department guaranteeing or intended to guarantee any Debt, leases, dividends or other obligations other than Power Obligations (any such Debt, leases, dividends or other obligations, the "primary obligations") of any other Person (the "primary obligor") in any manner, whether directly or indirectly, including, without limitation, any obligation of the Department, whether or not contingent, (a) to purchase any such primary obligation or any property constituting direct or indirect security therefor, (b) to advance or supply funds (i) for the purchase or payment of any such primary obligation or (ii) to maintain working capital or equity capital of the primary obligor or otherwise to maintain the net worth or solvency of the primary obligor, (c) to purchase property, securities or services primarily for the purpose of assuring the holder of any such primary obligation of the ability of the primary obligor to make payment of such primary obligation or (d) otherwise to assure or hold harmless the holder of such primary obligation against loss in respect thereof; provided, however, that the term Contingent Obligation shall not include endorsements of instruments for deposit or collection in the ordinary course of business. The amount of any Contingent Obligation shall be deemed to be an amount equal to the stated or determinable amount of the primary obligation in respect of which such Contingent Obligation is made or, if not stated or determinable, the maximum reasonably anticipated liability in respect thereof (assuming such Person is required to perform thereunder) as determined by the Department in good faith.

"Control" of a Person shall mean the power of another Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise, to direct or cause

the direction of the management and policies of such first Person. "Controlled" and "Controlling" shall have corresponding meanings.

"CPUC" shall mean the California Public Utility Commission.

"Credit Documents" shall mean this Agreement, each Bond, each Notice of Conversion, each Notice of Continuation, each Joinder, each Assignment and Acceptance Agreement and the Syndication Assignment and Acceptance Agreement.

"Debt" shall mean, without duplication, (a) all indebtedness (including principal, interest, fees and charges) of the Department for borrowed money, (b) the deferred purchase price of property or services (other than accrued expenses and current trade accounts payable incurred in the ordinary course of business) which in accordance with GAAP or SAP, as the case may be, would be shown on the liability side of the balance sheet of the Department, provided that amounts payable with respect to property and/or services which are included within the defined term "Operating and Maintenance Costs" shall not constitute "Debt," (c) the face amount of all letters of credit issued for the account of the Department and all drafts drawn thereunder to the extent issued in support of obligations which themselves are "Debt", (d) all obligations other than Power Obligations under conditional sale or other title retention agreements relating to property purchased by the Department, (e) all liabilities secured by any Lien on any property owned by the Department but not exceeding the fair market value of the property that is secured by any such Lien, whether or not such liabilities have been assumed by the Department, (f) the aggregate amount required to be capitalized under leases under which the Department is the lessee, (g) the amount of all indebtedness, obligations or other liabilities of the Department other than Power Obligations to its counter-parties in respect of interest rate and currency protection agreements (e.g., swaps, caps and collars) after netting out the amount of all indebtedness, obligations or other liabilities owed to the Department by its counter-parties in respect of such agreements (provided such net indebtedness, obligations and liabilities are greater than zero) and (h) all Contingent Obligations of the Department in respect of any indebtedness, obligations or liabilities of any other Person of the type referred to in clauses (a) through (g) of this definition. For purposes of calculating indebtedness, obligations and liabilities under interest rate and currency protection agreements, such calculation shall be made in accordance with market convention at the time of such calculation or, should an Event of Default or Event of Noncompliance have occurred and be continuing, in accordance with the definition of "Market Quotation" set forth in the Interest Rate and Currency Exchange Agreement of the International Swap Dealers Association, Inc. as in effect on the date hereof.

"Default" shall mean any event, act or condition which with notice or lapse of time or the making of a determination could, unless cured or waived, reasonably be expected to result in an Event of Default.

"Department" shall have the meaning provided in the introductory paragraph of this Agreement.

"Director" shall mean, at any time, the individual who, at that time, is the Director of the Department.

"Dollars" and the sign "$" shall each mean freely transferable lawful money of the United States.

"Effective Date" shall have the meaning provided in Section 9.15.

"Electric Power Fund" shall mean the Department of Water Resources Electric Power Fund originally established in the State treasury pursuant to Chapter 3 of the Statutes of 2001 (SB7 of the First 2001-02 Extraordinary Session) and as continued by Section 80200 of the Water Code, and referenced in the Executive Order.

"Electrical Corporation" shall have the meaning provided in Section 218 of the PUC as in effect on the date of this Agreement.

"Emergency Proclamation" shall mean the proclamation of the Governor made on January 17, 2001, that a state of emergency exists within the State due to existing energy shortages.

"Emergency Services Act" shall mean Chapter 7, Division 1, Title 2 of the California Government Code.

"Event of Default" shall have the meaning provided in Section 7.1.

"Event of Noncompliance" shall have the meaning provided in Section 7.2.

"Executive Order" shall mean Executive Order D-42-01 adopted by the Governor on June 18, 2001 pursuant to the Emergency Proclamation.

"Federal Funds Rate" shall mean, on any day, the rate per annum (rounded upward if necessary to the nearest one-hundredth of one percent) equal to the weighted average of the rate 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 published on such next succeeding Business Day, the Federal Funds Rate for such day shall be the average rate quoted to the Agent on such day on such transactions as reasonably determined by the Agent. Each change in the interest rate on a Base Rate Loan which results from a change in the Federal Funds Rate shall become effective on the day on which the change in the Federal Funds Rate becomes effective.

"Final Payment Date" shall have the meaning provided in Section 3.4.

"GAAP" shall mean generally accepted accounting principles as in effect from time to time in the United States and applicable to governmental units such as the Department.

"Governmental Authority" shall mean any nation or government, any state or other political subdivision thereof, any central bank (or similar monetary or regulatory authority) thereof, any entity or officer exercising executive, legislative, judicial, regulatory or administrative functions of or pertaining to government, and any corporation or other entity owned or

controlled, through stock or capital ownership or otherwise, by any of the foregoing. For the avoidance of doubt, the Governor shall be considered a Governmental Authority.

"Governmental Regulation" shall mean any (a) United States, state or foreign law, rule or regulation (including, without limitation, Regulation D); and (b) interpretation, application, directive or request applying to a class of lenders, including any Lender, of or under any United States, state or foreign law, rule or regulation (whether or not having the force of law) by any court or by any governmental, central banking, monetary or taxing authority charged with the interpretation or administration of such law, rule or regulation.

"Governor" shall mean the Governor of the State.

"Independent Consultant" shall mean a Person who or which is nationally recognized as being an expert in the supply and demand of electric power, and which Person is independent of the Department and the State. An Independent Consultant may be a Person regularly retained to provide services to the Department, but may not be an officer or an employee of the Department.

"Information" shall have the meaning provided in Section 5.9.

"Initial Lender" shall mean each Lender that is an initial signatory to this Agreement.

"Initial Period" shall mean the period from and including the date on which the Loans are made under this Agreement to but excluding the Term Out Period Commencement Date.

"Initial Written Determination" shall have the meaning provided in Section 4.1(b)(i).

"Interest and Fees Account" shall have the meaning provided in Section 2.11(c).

"Interest Determination Date" shall mean with respect to any LIBOR Loan the second Business Day prior to the commencement of any Interest Period relating to such LIBOR Loan.

"Interest Period" shall have the meaning provided in Section 2.7.

"Joinder" shall have the meaning provided in Section 9.15.

"Lead Arranger" shall mean J.P. Morgan Securities Inc., in its capacity as Lead Arranger and book manager.

"Legislature" shall mean the California State Assembly and the California State Senate.

"Lender" shall have the meaning provided in the first paragraph of this Agreement.

"Lender Affiliate" means, (a) with respect to any Lender, (i) an Affiliate of such Lender or (ii) any entity (whether a corporation, partnership, trust or otherwise) that is engaged in making, purchasing, holding or otherwise investing in bank loans and similar extensions of credit in the ordinary course of its business and is administered or managed by a Lender or an Affiliate of such Lender and (b) with respect to any Lender that is a fund which invests in bank loans and similar extensions of credit, any other fund that invests in bank loans and similar extensions of credit and

is managed by the same investment advisor as such Lender or by an Affiliate of such investment advisor.

"Lending Office" shall mean, with respect to each Lender, the office of such Lender specified as its "Lending Office" opposite its name on Schedule 2 or such other office or Affiliate of such Lender as such Lender may from time to time specify as such to the Department and the Agent.

"LIBOR" shall mean, with respect to an Interest Period, the rate equal to:

(a) the offered rate per annum for deposits in Dollars for a period equal to such Interest Period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on the Interest Determination Date for such Interest Period; or

(b) if clause (a) is inapplicable, the arithmetic mean (rounded upward if necessary to the nearest one-sixteenth of one percent) of the interest rates per annum offered by at least three prime rate banks selected by the Agent at approximately 11:00 a.m., London time, on the Interest Determination Date for such Interest Period for deposits in Dollars to prime banks in the London interbank market, in each case for a period equal to such Interest Period in an amount equal to the amount for which LIBOR is being determined.

"LIBOR Index" shall mean, for any seven consecutive day period commencing on a Wednesday and ending on the following Tuesday (or, in the case of the first reset period following the Closing Date, the eight consecutive day period commencing on June 26, 2001 and ending on July 3, 2001 (the "Initial Period")), the offered rate per annum for deposits in Dollars for a one month period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on Wednesday of the applicable seven-day period (or, in the case of the Initial Period, on Tuesday, June 26, 2001).

"LIBOR Loan" shall mean any Taxable Loan or portion thereof that is bearing interest based upon Adjusted LIBOR.

"Lien" shall mean any mortgage, pledge, hypothecation, assignment, deposit arrangement, encumbrance, lien (statutory or other), preference, priority or other security agreement of any kind or nature whatsoever (including, without limitation, any conditional sale or other title retention agreement, any financing or similar statement or notice filed under the UCC or any other similar recording or notice statute, and any lease having substantially the same effect as any of the foregoing).

"Loan" shall mean, as the context requires, a Taxable Loan, a Tax-Exempt Loan or both.

"Majority Lenders" shall mean, at any time, Lenders whose Pro Rata Shares in the aggregate exceed 60%.

"Material Adverse Effect" shall mean an event or occurrence, including, without limitation, a Change in Law, (a) the effect of which could reasonably be expected to have a material adverse effect on the ability of the Department to prescribe, revise or collect charges for electrical power, (b) which materially adversely affects the ability of the Department to timely perform its obligations under the Transaction Documents to which it is a party, (c) which materially adversely affects the enforceability of any Transaction Document, (d) which materially adversely affects the Liens, privileges, rights and remedies of the Agent or any Lender under the Transaction Documents or (e) which materially adversely affects the Collateral or the rights of the Lenders with respect thereto.

"Net Revenues" shall mean, at any time, the amount by which (a) the sum of the Revenues reasonably expected to be deposited in the Electric Power Fund during the next three calendar months and the moneys on deposit in or securities credited to the Interest and Fees Account and the Electric Power Fund which are reasonably expected to be available to pay Loans, Parity Debt and Operating and Maintenance Costs during such three-month period exceeds (b) the Operating and Maintenance Costs reasonably expected to be due and payable during that same period.

"Noncompliance" shall mean any event, act or condition which with notice or lapse of time or the making of a relevant determination could, unless cured or waived, reasonably be expected to result in an Event of Noncompliance.

"Notice of Continuation" shall have the meaning provided in Section 2.5(c).

"Notice of Conversion" shall have the meaning provided in Section 2.5(a).

"Notice Office" shall mean, (a) in the case of the Agent, the office of the Agent c/o J.P. Morgan Chase, 1 Chase Manhattan Plaza, 8th Floor, New York, New York 10081, Attention: Loan and Agency Services, Terri M. Williams, facsimile number: (212) 552-7409, telephone number: (212) 552-5777, with a copy to Morgan Guaranty Trust Company of New York, 60 Wall Street, New York, New York 10260, Attention: Municipal Credit Department, facsimile number (212) 648-5256, or such other office or offices as the Agent may hereafter designate in writing as such to the other parties hereto and (b) in the case of a Lender, the office set forth opposite the name of such Lender on Schedule 2, or such other office or offices as such Lender may hereafter designate in writing as such to the Agent and the Department.

"Obligations" shall mean all Loans, Bonds, advances, debt, principal, interest, fees, expenses, costs and other amounts owed to any Lender pursuant to the terms of this Agreement, any other Transaction Document, or any other document, instrument or agreement entered into by the Department with or in favor of any Lender in connection therewith, together with all guaranties, covenants and duties owing by the Department to any of the foregoing of any kind or description, whether direct or indirect, absolute or contingent, due or to become due, now existing or hereafter arising.

"Operating and Maintenance Costs" shall mean the Department's costs and expenses under power supply agreements (including termination and liquidated damage payments), payments under any security agreements executed in connection with power supply agreements, administrative and general expenses, insurance premiums, legal and engineering expenses, consulting and technical services, payments relating to fuel or electricity hedging instruments,

charges payable by the Department pursuant to any licenses, orders or mandates from any agency or regulatory body having lawful jurisdiction, rebate payments or yield reduction payments under Section 148 of the Internal Revenue Code and regulations thereunder, taxes, governmental charges, and any other expenses required to be paid by the Department, in each case only to the extent properly and directly attributable to any activities of the Department authorized pursuant to Division 27 of the Water Code and/or the Executive Order; the expenses, liabilities and compensation of the fiduciaries required to be paid pursuant to any agreement executed by the Department pursuant to Division 27 of the Water Code and/or the Executive Order; the Department's costs of avoiding purchasing power for retail end use customers pursuant to Division 27 of the Water Code and/or the Executive Order, including, without limitation, power rebate and power conservation programs; and in addition all costs and expenses arising from or in connection with the conduct of Department activities pursuant to Division 27 of the Water Code and/or the Executive Order which costs and expenses would constitute current operating expenses under GAAP or SAP, as the case may be; provided, however, so long as any Loans or Parity Debt remain outstanding, Operating and Maintenance Costs shall not include State Reimbursement Claims.

"Originator" shall have the meaning provided in Section 9.4(g).

"Owner" shall mean the registered owner of any Bond as shown on the books for the registration and transfer of Bonds maintained in accordance with Section 2.3.

"Parent" shall have the meaning provided in Section 2.8(b).

"Parity Debt" shall mean that amount of bond anticipation notes and/or commercial paper issued by the Department prior to the Term Out Period Commencement Date and secured by the Water Code Collateral ("New Debt") which, when added to the sum of the aggregate outstanding principal amount of Loans then outstanding (after giving effect to any voluntary prepayment of Loans to be made from the proceeds of such New Debt), is equal to or less than $6,000,000,000; provided, however, if Parity Debt comprises commercial paper, commercial paper issued solely to pay maturing commercial paper will also be classified as "Parity Debt." Similarly, if any Parity Debt is enhanced by credit and/or liquidity support, any payment obligation of the Department to the provider of such credit and/or liquidity support in respect of advances made in respect of such Parity Debt will also be classified as "Parity Debt" so long as such payment obligation is amortized no more rapidly than the installment payment schedule set forth in Section 3.4.

"Participant" shall have the meaning provided in Section 9.4(g).

"Payment Account" shall mean such account as the Agent may hereafter from time to time designate in writing as such to the Department and the Lenders, which account shall initially be ABA #: 021-000-021, Account #: 323-2-23788, Account Name: California Department of Water Resources, maintained by the Agent at the Payment Office.

"Payment Office" shall mean the office of the Agent c/o Chase Manhattan Bank, 1 Chase Manhattan Plaza, 8th Floor, New York, New York 10081, or such other office as the Agent may hereafter designate in writing as such to the other parties hereto.

"Permitted Debt" shall mean any Debt permitted pursuant to Section 6.9, including Parity Debt.

"Person" shall mean any individual, partnership, limited liability company, joint venture, firm, corporation, association, trust or other enterprise or any government or political subdivision or any agency, department or instrumentality thereof.

"Power Obligations" shall mean contractual obligations of the Department arising from or under (a) power supply agreements and fuel agreements that are entered into by the Department pursuant to Division 27 of the Water Code and/or the Executive Order pursuant to which Persons agree to supply power and/or fuel, as the case may be, to or on behalf of the Department and (b) power hedging arrangements and fuel hedging arrangements that are entered into by the Department pursuant to Division 27 of the Water Code and/or the Executive Order in order to manage the Department's electric power purchase program contemplated by Division 27 of the Water Code and the Executive Order.

"Prime Rate" shall mean the rate which Morgan Guaranty Trust Company of New York announces from time to time in New York, New York as its prime lending rate, the Prime Rate to change when and as such prime lending rate changes. The Prime Rate is a reference rate and does not necessarily represent the lowest or best rate actually charged to any customer.

"Pro Rata Share" shall mean, as to any Lender at any time, the percentage equivalent (rounded to the third decimal place) at such time of the aggregate unpaid principal amount of the Loans of such Lender divided by the aggregate unpaid principal amount of the Loans of all Lenders.

"Properly Structured Charge" shall have the meaning provided in Section 6.8.

"PUC" shall mean the California Public Utilities Code.

"Rate Agreement" shall mean an agreement between the Department and the CPUC contemplated by Section 80110 of the Water Code which is in form and substance satisfactory to the Majority Lenders.

"Regulation D" shall mean Regulation D of the Board of Governors of the Federal Reserve System as from time to time in effect and any successor to all or a portion thereof establishing reserve requirements.

"Regulatory Change" means, with respect to any Lender, any change on or after the date of this Agreement in any Governmental Regulation, including, without limitation, the introduction of a new Governmental Regulation or the rescission of an existing Governmental Regulation.

"Reserve Requirement Rate" shall mean, for any Interest Period, the aggregate of the rates, effective as of the Interest Determination Date for such Interest Period, at which:

(a) reserves (including any marginal, emergency, supplemental, special or other reserves) are required to be maintained during such Interest Period under Regulation D

against "Eurocurrency liabilities" (as such term is used in Regulation D) by member banks of the Federal Reserve System; and

(b) any additional reserves are required to be maintained by any Lender by reason of any Regulatory Change against (x) any category of liabilities which includes deposits by reference to which LIBOR is to be determined or (y) any category of any of credit or other assets which include LIBOR Loans.

"Revenue Requirement" shall mean the amount from time to time conveyed by the Department to the CPUC as being the amount needed by the Department to satisfy its obligations under Section 80134 of the Water Code and the Executive Order.

"Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to AB1X and/or the Executive Order.

"SAP" shall mean statutory accounting principles as in effect from time to time and applicable to governmental units such as the Department.

"Satisfactory Purchase Contracts" shall mean one or more contracts between the Department and power producers or suppliers pursuant to which the Department will purchase electric power for sale to retail end-use customers as contemplated by Division 27 of the Water Code and/or the Executive Order, and from which the Department reasonably determines to the satisfaction of the Super Majority Lenders that it will be entitled to recover the Revenues sufficient to satisfy its obligations under this Agreement, including without limitation Section 6.8 hereof.

"Secondary Closing Date" shall mean the first date on which all of the conditions precedent specified in Section 4.2 have been satisfied or waived by the Agent and the Additional Lenders that have agreed to make Loans on such date.

"Secondary Written Determination" shall have the meaning provided in Section 4.2(b)(i).

"Servicing Agreement" shall mean, with respect to an Electrical Corporation, the servicing agreement between the Department and such Electrical Corporation contemplated by Section 80106(a) of the Water Code which is in form and substance satisfactory to the Majority Lenders.

"Servicing Order" shall mean an order issued by the CPUC as contemplated by Section 80106(b) of the Water Code which is in form and substance satisfactory to the Majority Lenders.

"State" shall mean the State of California.

"State Reimbursement Claims" shall mean all claims of the State or any department, agency or other instrumentality thereof for reimbursement of amounts expended on behalf of the Department or otherwise, or appropriated to the Department or any other Governmental Authority, by the State to purchase electric power.

"Sunset Date" shall mean the date set forth in Section 80260 of the Water Code and Section 24 of the Emergency Regulations which at the date of this Agreement is January 1, 2003.

"Super Majority Lenders" shall mean, at any time, Lenders whose Pro Rata Shares in the aggregate exceed 75%.

"Syndication Agreement" shall mean the Syndication Agreement of even date herewith among the Lead Arranger and the Initial Lenders.

"Syndication Assignment and Acceptance Agreement" shall have the meaning provided in the Syndication Agreement.

"Syndication Period" shall mean the period commencing on the Term Out Period Commencement Date and ending at 4:00 P.M. on the one hundred twentieth day thereafter.

"Taxable Bond" and "Taxable Bonds" shall have the meanings provided in Section 2.3(a).

"Taxable Commitment" shall mean for (a) each Initial Lender, at the Closing Date, and (b) each Additional Lender, at the applicable Secondary Closing Date, the amount set forth opposite such Lender's name in Schedule 1 under the heading "Taxable Commitment".

"Taxable Loan" and "Taxable Loans" shall have the meanings provided in Section 2.1(a).

"Tax-Exempt Bond" and "Tax-Exempt Bonds" shall have the meanings provided in Section 2.3(b) and shall include any Tax-Exempt Bonds that are substituted for Taxable Bonds pursuant to Section 9.19.

"Tax-Exempt Commitment" shall mean for (a) each Initial Lender, at the Closing Date, and (b) each Additional Lender, at the applicable Secondary Closing Date, the amount set forth opposite such Lender's name in Schedule 1 under the heading "Tax-Exempt Commitment".

"Tax-Exempt Lender" shall have the meaning provided in Section 9.4(i).

"Tax-Exempt Loan" and "Tax-Exempt Loans" shall have the meanings provided in Section 2.1(b) and shall include any Tax-Exempt Loans that are substituted for Taxable Loans Bonds pursuant to Section 9.19.

"Taxes" shall have the meaning provided in Section 3.6.

"Term Out Final Period" shall mean the period from and including the twelve month anniversary of the Term Out Period Commencement Date to but excluding the date on which all outstanding Obligations are paid in full.

"Term Out First Period" shall mean the period from and including the Term Out Period Commencement Date to but excluding the six month anniversary of the Term Out Period Commencement Date.

"Term Out Period Commencement Date" shall mean October 31, 2001.

"Term Out Second Period" shall mean the period from and including the six month anniversary of the Term Out Period Commencement Date to but excluding the twelve month anniversary of the Term Out Period Commencement Date.

"Transaction Documents" shall mean the Credit Documents and the letter agreements regarding fees described in Section 3.1(d).

"Treasurer" shall mean the Treasurer of the State.

"UCC" or "Uniform Commercial Code" shall mean the Uniform Commercial Code as from time to time in effect in the relevant jurisdiction.

"United States" and "U.S." shall each mean the United States of America.

"Water Code" shall mean the California Water Code.

"Water Code Bonds" shall have the meaning given to the term "bonds" set forth in the Section 80010(a) of the Water Code.

"Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue.

1.2. Principles of Construction.

(a) All references to sections, schedules and exhibits are to sections, schedules and exhibits in or to this Agreement unless otherwise specified.

(b) The words "hereof," "herein" and "hereunder" and words of similar import when used in this Agreement shall refer to this Agreement as a whole and not to any particular provision of this Agreement.

(c) References in the Transaction Documents to any of the "Department", the "State", the "Agent" or the "Lenders" shall be construed so as to include their respective successors and permitted assigns and, in the case of the Department any Person that, by operation of law, succeeds to all of the duties and obligations of the Department under AB1X and/or the Executive Order.

(d) References in the Transaction Documents to a "law" shall be construed to mean any law, including common or customary law and any constitution, decree, judgment, legislation, order, ordinance, regulation, rule, statute, treaty or other legislative or regulatory measure, in each case of any jurisdiction.

(e) References in the Transaction Documents to a statute shall unless otherwise specified be construed as a reference to such statute as amended, modified or reenacted from time to time.

(f) A time of day is, unless otherwise stated, a reference to New York, New York time.

(g) Unless otherwise specified, any reference in the Transaction Documents to another agreement shall be construed as a reference to that other agreement as the same may have been, or may from time to time be, amended or supplemented.

(h) The headings of the several sections and subsections of the Transaction Documents are inserted for convenience only and shall not in any way affect the meaning or construction of any provision of any Transaction Document.

(i) In the computation of periods of time from a specified date to a later specified date, the word "from" means "from and including", the words "to" and "until" each mean "to but excluding", and the word "through" means "to and including".

(j) Unless otherwise expressly provided, any reference to any action of the Agent or any Lender by way of consent, approval or waiver shall be deemed modified by the phrase "in its/their sole discretion".

(k) This Agreement and the other Transaction Documents are the result of negotiations among and have been reviewed by counsel to the Agent, the Lenders and the Department, and are the products of all parties. Accordingly, they shall not be construed against the Agent or the Lenders merely because of the Agent's or the Lenders' involvement in their preparation.

(l) All words importing any gender shall be deemed to include the other genders.

(m) If the Director of the Department delivers a written notice to the Agent and the Initial Lenders designating one or more officers of the Department to serve as Authorized Representatives, such designation shall become effective, and such officers shall be treated as Authorized Representatives under the Transaction Documents, at the commencement of business on the Business Day following the day on which such notice is received by the Agent. The Agent and each Lender shall be entitled to rely, without investigation, on any action taken under the Transaction Documents by a Person who, at the time such action is taken, is an Authorized Representative.

SECTION 2. LOAN FACILITY; SECURITY INTEREST

2.1. Loans; Additional Commitments.

(a) Subject to, and upon, the terms and conditions set forth herein, each Initial Lender with a Taxable Commitment and each Additional Lender with an Additional Taxable Commitment severally agrees to make a loan (any such loan made by any Initial Lender or Additional Lender, a "Taxable Loan" and all such loans made by all the Initial Lenders and Additional Lenders, the "Taxable Loans") to the Department in an amount equal to such Initial Lender's Taxable Commitment and such Additional Lender's Additional Taxable Commitment, as the case may be. Taxable Loans shall bear interest as provided in Section 2.6 and once paid or prepaid may not be reborrowed. Taxable Loans shall initially be made as Base Rate Loans.

(b) Subject to, and upon, the terms and conditions set forth herein, each Initial Lender with a Tax-Exempt Commitment and each Additional Lender with an Additional Tax-Exempt Commitment severally agrees to make, or cause to be made, a loan (any such loan made or caused to be made by any Initial Lender or Additional Lender, a "Tax-Exempt Loan" and all such loans made by all the Initial Lenders and Additional Lenders, the "Tax-Exempt Loans") to the Department in an amount equal to such Initial Lender's Tax-Exempt Commitment and such Additional Lender's Additional Tax-Exempt Commitment, as the case may be. Tax-Exempt Loans shall bear interest as provided in Section 2.6 and once paid or prepaid may not be reborrowed.

(c) If, on and after the Closing Date and prior to July 31, 2001, the Agent and the Lead Arranger receives a written firm commitment from a prospective Lender (each, an "Additional Lender") to make an advance or advances to the Department hereunder, the Department shall have the option, in consultation with the Agent and the Lead Arranger, to accept all or a portion of such new commitment, provided that the sum of (A) such new commitment, (B) the then aggregate total amount of all Commitment(s) or the then outstanding Loans, as the case may be, and (C) and the total amount of all accepted commitments for Parity Debt or then outstanding Parity Debt, as the case may be, shall not exceed $6,000,000,000; and provided further that the Dollar amount of the commitment or portion thereof that is accepted is not less than $10,000,000 and integral multiples of $5,000,000 in excess thereof. The Dollar value of each such accepted commitment is referred to herein as an "Additional Commitment." Each Additional Commitment may be a commitment to make either a Taxable Loan (an "Additional Taxable Commitment") or a Tax-Exempt Loan (an "Additional Tax-Exempt Commitment") or both types of Loans. Each Additional Lender shall become a "Lender" under this Agreement by executing and delivering to the Department and the Agent a joinder to this Agreement in accordance with Section 9.15. Promptly following its receipt of an executed joinder to this Agreement, the Agent shall prepare and deliver to the Department and each Lender (including each Additional Lender) revised Schedules 1 and 2 reflecting the Additional Taxable Commitment and/or Additional Tax-Exempt Commitment of such Additional Lender, as the case may be, and the notice information for such Additional Lender. The Taxable Loan, if any, made by any Additional Lender shall be comprised of a Base Rate Loan and LIBOR Loans in the same proportion as the then existing Lenders' Taxable Loans and each Taxable Loan made by an Additional Lender shall bear interest at the same rate as the corresponding Base Rate Loan and LIBOR Loans of the then existing Lenders. The Tax-Exempt Loan, if any, made by any Additional Lender shall bear interest at the same rate as the Tax-Exempt Loan of the then existing Lenders. The Department agrees to compensate each Additional Lender, upon the written request thereof through the Agent, for any loss, cost or expense which such Additional Lender reasonably determines to be attributable in accordance with Section 2.10 to the making of its Loan(s) pursuant to this Section 2.1(c).

2.2. Disbursement of Funds.

(a) So long as the conditions precedent specified in Section 4.1 are satisfied or waived by the Agent and the Initial Lenders on or prior to 12:00 Noon on a Business Day, each Initial Lender will make available, or cause to be made available, by 3:00 PM on such day the full amount of its Commitment less the amount of any fees owing by the Department to such Lender on or before such day in Dollars and in immediately available funds at the Payment Account of the Agent, and the Agent will make available to the Department at its Payment Office the aggregate

of the amounts so made available, or caused to be made available, by the Initial Lenders less the Capitalized Interest and Fees Amount applicable to the Commitments of the Initial Lenders. If the conditions precedent specified in Section 4.1 are satisfied or waived by the Agent and the Initial Lenders after 12:00 Noon on a Business Day, each Initial Lender will make available, or cause to be made available, by 12:00 Noon on the next Business Day the full amount of its Commitment less the amount of any fees owing by the Department to such Lender on or before such day in Dollars and in immediately available funds at the Payment Account of the Agent, and the Agent will make available to the Department at its Payment Office the aggregate of the amounts so made available, or caused to be made available, by the Initial Lenders less the Capitalized Interest and Fees Amount applicable to the Commitments of the Initial Lenders.

(b) So long as the conditions precedent specified in Section 4.2 are satisfied or waived by the Agent and the Additional Lenders on or prior to 12:00 Noon on a Business Day, each Additional Lender will make available by 3:00 PM on such day the full amount of its Additional Commitment less the amount of any fees owing by the Department to such Lender on or before such day in Dollars and in immediately available funds at the Payment Account of the Agent, and the Agent will make available to the Department at its Payment Office the aggregate of the amounts so made available by such Additional Lenders less the Capitalized Interest and Fees Amount applicable to the Additional Commitments of the Additional Lenders. If the conditions precedent specified in Section 4.2 are satisfied or waived by the Agent and the Additional Lenders after 12:00 Noon on a Business Day, each Additional Lender will make available by 12:00 Noon on the next Business Day the full amount of its Additional Commitment less the amount of any fees owing by the Department to such Lender on or before such day in Dollars and in immediately available funds at the Payment Account of the Agent, and the Agent will make available to the Department at its Payment Office the aggregate of the amounts so made available by such Additional Lenders less the Capitalized Interest and Fees Amount applicable to the Additional Commitments of the Additional Lenders.

2.3. Bonds.

(a) The Department's obligation to pay the principal of, and interest on, the Taxable Loan made by each Initial Lender with a Taxable Commitment and each Additional Lender with an Additional Taxable Commitment, as the case may be, shall be evidenced by a note duly executed and delivered to such Lender by the Department substantially in the form of Exhibit A with blanks appropriately completed in conformity herewith (each a "Taxable Bond" and, collectively, the "Taxable Bonds").

(b) The Department's obligation to pay the principal of, and interest on, the Tax-Exempt Loan made by each Initial Lender with a Tax-Exempt Commitment and each Additional Lender with an Additional Tax-Exempt Commitment, as the case may be, shall be evidenced by a note duly executed and delivered to or upon the order of such Lender by the Department substantially in the form of Exhibit B with blanks appropriately completed in conformity herewith (each a "Tax-Exempt Bond" and, collectively, the "Tax-Exempt Bonds").

(c) Each Lender will note on its internal records the amount of each Loan made by it and each payment in respect thereof and will, prior to any transfer of any of its Bonds, endorse on

the reverse side thereof the outstanding principal amount of the Loans evidenced thereby. Failure to make any such notation shall not affect the Department's obligations in respect of such Loans.

(d) Bonds shall be issued in the form of fully registered Bonds without coupons. Bonds may have such letters, numbers or other marks of identification and such legends and endorsements placed thereon as may be required to comply with any applicable laws or rules or regulations, or as may, consistent herewith, be determined by the officers executing such Bonds, as evidenced by their execution of the Bonds. Any portion of the text of any Bond may be set forth on the reverse thereof, with an appropriate reference thereto on the face of such Bond, or as multiple pages (with or without such a reference). Bonds may be typewritten, printed, engraved, lithographed or otherwise produced. The Bonds shall be executed in the name of the Department by the manual or facsimile signature of an Authorized Representative.

(e) Bonds, upon surrender thereof to the Department with a written instrument of transfer satisfactory to the Department, duly executed by the Owner or such Owner's duly authorized attorney, may, at the option of such Owner but subject to the restrictions set forth in Section 9.4, be exchanged for an equal aggregate principal amount of Bonds of the same interest rate in denominations of $10,000,000 or integral multiples thereof.

(f) So long as any of the Bonds shall remain outstanding, the Department shall maintain and keep books for the registration and transfer of Bonds; and, upon presentation thereof for such purpose, the Department shall register or cause to be registered therein, and permit to be transferred thereon, under such reasonable regulations as it may prescribe, any Bond entitled to registration or transfer pursuant to Section 9.4. So long as any of the Bonds remain outstanding, the Department shall make all necessary provision to permit the exchange of Bonds at the office of the Department.

(g) Except as may be otherwise provided in Section 9.4 hereof, each Bond shall be transferable only upon the books of the Department by the Owner thereof in person or by such Owner's attorney duly authorized in writing, upon surrender thereof together with a written instrument of transfer satisfactory to the Department duly executed by the Owner or such Owner's duly authorized attorney. Upon the transfer of any such Bond, the Department shall issue in the name of the transferee a new Bond or Bonds of the same aggregate principal amount and interest rate as the surrendered Bond.

(h) The Department may deem and treat the Person in whose name any Bond shall be registered upon the books of the Department as the absolute owner of such Bond, whether such Bond shall be overdue or not, for the purpose of receiving payment of, or on account of, the principal of and interest on such Bond and for all other purposes, and all such payments so made to any such registered owner or upon such Owner's order shall be valid and effectual to satisfy and discharge the liability upon such Bond to the extent of the sum or sums so paid, and the Department shall not be affected by any notice to the contrary.

(i) In case any Bond shall become mutilated or be destroyed, stolen or lost, the Department shall execute and deliver a new Bond of like interest rate and principal amount as the Bond so mutilated, destroyed, stolen or lost, in exchange and substitution for such mutilated Bond, upon surrender and cancellation of such mutilated Bond, or in lieu of and substitution for the Bond destroyed, stolen or lost, upon filing with the Department evidence satisfactory to the

Department that such Bond has been destroyed, stolen or lost and proof of ownership thereof, and upon furnishing the Department with indemnity satisfactory to it and complying with such other reasonable regulations as the Department may prescribe. All Bonds so surrendered to the Department shall be canceled by it. Any such new Bonds issued in substitution for Bonds alleged to be destroyed, stolen or lost shall constitute original additional contractual obligations on the part of the Department, whether or not the Bonds so alleged to be destroyed, stolen or lost be at any time enforceable by anyone.

(j) All Bonds that have been paid (whether at maturity or otherwise) or delivered to the Department for cancellation shall be canceled and not reissued.

2.4. Severable Obligation. It is understood that no Lender shall be responsible for any default by any other Lender of its obligation to make Loans hereunder and that each Lender shall be obligated to make the Loans provided to be made by it hereunder regardless of the failure of any other Lender to make its Loans hereunder.

2.5. Conversions and Continuations of Taxable Loans.

(a) Prior to the Term Out Period Commencement Date, the Department shall have the option to convert on any Business Day all or a portion of the outstanding principal amount of the Taxable Loans from LIBOR Loans to Base Rate Loans and vice versa (all such conversions of Base Rate Loans thereof shall be incurred from the Lenders with Taxable Loans *pro rata* on the basis of the unpaid principal balance of each Lenders' Taxable Loan), provided that (i) except as otherwise provided in Section 2.9(b), LIBOR Loans may be converted into Base Rate Loans only on the last day of the Interest Period applicable to the LIBOR Loans being converted and no partial conversion of LIBOR Loans shall reduce the outstanding principal amount of the remaining LIBOR Loans of all Lenders to less than $50,000,000 and integral multiples of $5,000,000 in excess thereof; (ii) Base Rate Loans may only be converted into LIBOR Loans if no Default, Event of Default, Noncompliance or Event of Noncompliance is in existence on the date of the conversion; (iii) Base Rate Loans of all Lenders may only be converted into LIBOR Loans in a minimum amount of $50,000,000 and integral multiples of $5,000,000 in excess thereof; and (iv) no conversion pursuant to this Section 2.5(a) shall result in more than four different LIBOR Loans existing on any date. Each such conversion shall be effected by the Department by giving the Agent at its Notice Office prior to 11:00 a.m. at least three Business Days' prior notice in the form of Exhibit C (each a "Notice of Conversion") signed by an Authorized Representative specifying the Taxable Loans to be so converted and, if Base Rate Loans are to be converted into LIBOR Loans, the initial Interest Period to be applicable thereto. The Agent shall promptly give each Lender notice of any proposed conversion affecting any of its Taxable Loans.

(b) Unless previously converted to Base Rate Loans or prepaid in full, subject to Section 2.10, all LIBOR Loans shall be automatically converted, without further action on the part of any Person, to Base Rate Loans on the Term Out Period Commencement Date.

(c) Prior to the Term Out Period Commencement Date, the Department shall have the option to continue all or a portion (which portion shall not be less than $50,000,000 and integral multiples of $5,000,000 in excess thereof) of the outstanding principal amount of LIBOR Loans of all Lenders as LIBOR Loans after the last day of the then current Interest Period, provided that

(i) no Default, Event of Default, Noncompliance or Event of Noncompliance exists on the date of continuation; and (ii) no continuation pursuant to this Section 2.5(c) shall result in more than four different LIBOR Loans existing on any date. Each such continuation (or, if the notice described below so specifies, successive continuations) shall be effected by the Department by giving the Agent at its Notice Office prior to 11:00 a.m. at least three Business Days' prior notice in the form of Exhibit D (each a "Notice of Continuation") signed by an Authorized Representative specifying the LIBOR Loans to be so continued and the subsequent Interest Period applicable thereto. The Agent shall promptly give each Lender notice of any proposed continuation affecting any of its LIBOR Loans.

2.6. Interest; Overdue Amounts.

(a) Subject to Section 2.6(d), the Department agrees to pay interest in respect of the unpaid principal amount of each Base Rate Loan from the date the proceeds thereof are made available to the Department until the earlier of (i) the date such Loan is repaid in full (whether by prepayment or otherwise) and (ii) the maturity thereof at a rate per annum which shall be the Base Rate in effect from time to time plus the Applicable Margin.

(b) Subject to Section 2.6(d), prior to the Term Out Period Commencement Date, the Department agrees to pay interest in respect of the unpaid principal amount of each LIBOR Loan from the date the proceeds thereof are made available to the Department until the earliest of (i) the Term Out Period Commencement Date, (ii) the date such Loan is repaid in full (whether by prepayment or otherwise) and (iii) the maturity thereof at a rate per annum which shall, during each Interest Period applicable thereto, be 0.75% in excess of the Adjusted LIBOR for such Interest Period.

(c) Subject to Section 2.6(d), prior to the Term Out Period Commencement Date, the Department agrees to pay interest in respect of the unpaid principal amount of each Tax-Exempt Loan from the date the proceeds thereof are made available to the Department until the earliest of (i) the Term Out Period Commencement Date, (ii) the date such Loan is repaid in full (whether by prepayment or otherwise) and (iii) the maturity thereof at a rate per annum which shall be the sum of (A) 80% of the LIBOR Index and (B) 0.75%. Subject to Section 2.6(d), on and after the Term Out Period Commencement Date, the Department agrees to pay interest in respect of the unpaid principal amount of each Tax-Exempt Loan from the Term Out Period Commencement Date until the earlier of (x) the date such Loan is repaid in full (whether by prepayment or otherwise) and (y) the maturity thereof (whether by acceleration or otherwise) at a rate per annum which shall be the Base Rate in effect from time to time plus the Applicable Margin.

(d) Overdue principal and, to the extent permitted by law, overdue interest in respect of each Loan and any other overdue amount payable by the Department hereunder shall bear interest at a rate per annum equal to 2% per annum in excess of the otherwise applicable interest rate (or, if no rate is in effect therefor, the per annum rate shall be the Base Rate plus 2%). During the continuance of an Event of Default or an Event of Noncompliance, each Loan and other amount payable by the Department hereunder shall bear interest at a rate per annum equal to 2% per annum in excess of the interest rate in effect therefor immediately prior to the occurrence of such Event of Default or Event of Noncompliance (or, if no rate is in effect therefor, the per annum rate shall be the Base Rate plus 2%).

(e) Accrued (and theretofore unpaid) interest shall be payable, (i) in respect of each Base Rate Loan and, after the Term Out Period Commencement Date, each Tax-Exempt Loan, quarterly in arrears on the last Business Day of each March, June, September and December and on the date such Base Rate Loan is converted to a LIBOR Loan; (ii) in respect of each LIBOR Loan, on the last day of each Interest Period applicable thereto; (iii) in respect of each Tax-Exempt Loan on or before the Term Out Commencement Date, monthly in arrears on the first Business Day of each calendar month and on the Term Out Commencement Date; and (iv) in respect of each Loan, on the date of any prepayment (on the amount prepaid), on any scheduled payment date, at maturity (whether by acceleration or otherwise) and, after such maturity, on demand.

2.7. Interest Periods. At the time it gives any Notice of Conversion in respect of the conversion of any Base Rate Loans or portion thereof into any LIBOR Loan and at the time it gives any Notice of Continuation in respect of the continuation into any LIBOR Loan, the Department shall have the right to elect, by giving the Agent notice thereof, the interest period (each an "Interest Period") applicable to such LIBOR Loan, which Interest Period shall, at the option of the Department, be (x) a fourteen day, one, two or three month period and, (y) if the Department has executed and delivered a bond purchase agreement pursuant to which the Department has agreed, subject to customary terms and conditions, to sell Water Code Bonds the proceeds of which will be used, in whole or in part, to repay all amounts owing under this Agreement, a seven day period, provided that: (a) the initial Interest Period for any LIBOR Loan shall commence on the date of any conversion thereof from a Base Rate Loan and each Interest Period occurring thereafter in respect of such Loan shall commence on the day on which the next preceding Interest Period applicable thereto expires; (b) if any Interest Period relating to a LIBOR Loan begins on a day for which there is no numerically corresponding day in the calendar month at the end of such Interest Period, such Interest Period shall end on the last Business Day of such calendar month; (c) if any Interest Period would otherwise expire on a day which is not a Business Day, such Interest Period shall expire on the next succeeding Business Day, provided that if any Interest Period for a LIBOR Loan would otherwise expire on a day which is not a Business Day but is a day of the month after which no further Business Day occurs in such month, such Interest Period shall expire on the next preceding Business Day; and (d) no Interest Period in respect of a LIBOR Loan shall extend beyond the Term Out Period Commencement Date. If upon the expiration of any Interest Period applicable to a LIBOR Loan, the Department has failed to elect a new Interest Period to be applicable to such LIBOR Loan as provided above, the Department shall be deemed to have elected to convert such Loan into a fourteen day LIBOR Loan effective as of the expiration date of such current Interest Period.

2.8. Increased Costs.

(a) If, on or after the date hereof, the adoption of any law, rule or regulation, or any change therein, or in the interpretation or administration thereof by any court, governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by any Lender with any request or directive made on or after the date hereof (whether or not having the force of law) of any such authority, central bank or comparable agency:

(i) shall subject such Lender to any tax, duty or other charge with respect to this Agreement or any Loans made by such Lender, or shall change the basis of taxation of

payments to such Lender of any amounts due under this Agreement or any Loans made by such Lender (except for changes in the rate of tax on the overall net income of such Lender); or

(ii) shall impose, modify or deem applicable any reserve (including, without limitation, any such requirement imposed by the Board of Governors of the Federal Reserve System), or similar requirement against the assets of, deposits with or for the account of, or credit extended by, such Lender or shall impose on such Lender any other condition affecting its obligations under this Agreement or its Loans;

and the result of any of the foregoing is to increase the cost to such Lender of performing its obligations under this Agreement, or to reduce the amount of any sum received or receivable by such Lender under this Agreement or any Loans made by such Lender hereunder, by an amount deemed by such Lender to be material, then, within 30 days after demand by such Lender (or, if such increased costs will continue to be incurred by such Lender, in arrears on a monthly basis), the Department shall pay to such Lender such additional amount or amounts as will compensate such Lender for such increased cost or reduction. Notwithstanding anything to the contrary contained in this Section 2.8(a), no Lender shall be entitled to claim any increased cost under this Section 2.8(a) in respect of its LIBOR Loans if such increased cost results in a change in reserve requirements which is reflected in an increase in the Reserve Requirement Rate.

(b) If a Lender shall have determined that, after the date hereof, the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency, has or would have the effect of reducing the rate of return on capital of such Lender (or of any Person controlling such Lender (a "Parent")) relating to such Lender's obligations hereunder or under any Loan made by such Lender, and such adoption, change, request or directive (taking into consideration its policies with respect to capital adequacy) will reduce such Lender's or Parent's rate of return on capital, then from time to time, within 30 days after demand by such Lender (with a copy to the Agent) (or if such additional costs of such Lender will continue to be suffered by such Lender, in arrears on a monthly basis as agreed between the Department and such Lender), the Department shall pay to such Lender such additional amount or amounts as will compensate such Lender (or its Parent) for such reduction in return.

(c) Each Lender will use commercially reasonable efforts to notify the Department within 30 days of such Lender's obtaining knowledge of any event occurring after the date hereof which would entitle such Lender (or its Parent) to compensation pursuant to this Section; provided that the failure of a Lender to notify the Department within such 30 day period shall not relieve the Department from any liability for payment of such compensation. A certificate of a Lender claiming compensation under this Section and setting forth the additional amount or amounts to be paid to it hereunder and attaching such information in reasonable detail as may be reasonably requested by the Department shall be conclusive in the absence of manifest error. In determining such amount, a Lender may use any reasonable average and attribution methods.

(d) No Participant shall be entitled to receive any greater payment under this Section than the Lender from whom such Participant acquired its participation interest would have been entitled to receive with respect to the rights transferred, unless such transfer is made with the Department's prior written consent.

2.9. Illegality, etc.

(a) In the event that any Lender shall have determined (which determination shall, absent manifest error, be final and conclusive and binding upon all parties hereto but, with respect to clause (i) below, may be made only by the Agent):

(i) on any Interest Determination Date for Taxable Loans that, by reason of any changes arising after the date of this Agreement affecting the interbank Eurodollar market, adequate and fair means do not exist for ascertaining the applicable interest rate on any basis provided for in the definition of LIBOR; or

(ii) at any time, that (x) the conversion of any Base Rate Loan (or portion thereof) into a LIBOR Loan or (y) the continuation of a LIBOR Loan has been made (A) unlawful by any law or governmental rule, regulation or order, (B) impossible by compliance by such Lender with any governmental request (whether or not having force of law) or (C) impracticable as a result of a contingency occurring after the date of this Agreement which materially and adversely affects the interbank Eurodollar market;

then, and in any such event, such Lender (or, in the case of clause (i) above, the Agent) shall promptly give notice (by telephone confirmed in writing) to the Department and, except in the case of clause (i) above, to the Agent of such determination (which notice the Agent shall promptly transmit to each of the other Lenders). Thereafter (x) in the case of clause (i) above, LIBOR Loans shall no longer be available until such time as the Agent notifies the Department and the Lenders that the circumstances giving rise to such notice by the Agent no longer exist, and any Notice of Conversion given by the Department with respect to Base Rate Loans (or portions thereof) which have not yet been converted to LIBOR Loans or any Notice of Continuation given by the Department with respect to the continuation of LIBOR Loans shall be deemed rescinded by the Department, and (y) in the case of clause (ii) above, take one of the actions specified in Section 2.9(b) as promptly as possible and, in any event, within the time period required by law.

(b) At any time that any LIBOR Loan is affected by the circumstances described in Section 2.9(a)(ii), the Department shall either (i) if the affected LIBOR Loan is then being made pursuant to a conversion, cancel said conversion by giving the Agent notice by telephone (confirmed in writing) of the cancellation on the same date that the Department was notified by the Lender or the Agent pursuant to Section 2.9(a)(ii) or (ii) if the affected LIBOR Loan is then outstanding, upon at least three Business Days' written notice to the Agent, require the affected Lender to convert such LIBOR Loan into a Base Rate Loan, provided that, if more than one Lender is affected at any time, then all affected Lenders must be treated the same pursuant to this Section 2.9(b).

2.10. Compensation. The Department shall compensate each Lender, upon its written request (which request shall set forth the basis for requesting such compensation and shall, absent

manifest error, be final and conclusive and binding on all the parties hereto), for all reasonable losses, expenses and liabilities (including, without limitation, any loss, expense or liability incurred by reason of the liquidation or reemployment of deposits or other funds required by such Lender to fund its LIBOR Loans) which such Lender may sustain: (a) if for any reason (other than a default by such Lender or the Agent) a conversion from or into, or continuation of, LIBOR Loans does not occur on a date specified therefor in a Notice of Conversion or Notice of Continuation (whether or not withdrawn by the Department or deemed rescinded pursuant to Section 2.9(a)); (b) if any repayment (including any prepayment made pursuant to Section 3.2 or 3.3) or conversion of any of its LIBOR Loans occurs on a date which is not the last day of an Interest Period with respect thereto; (c) if any prepayment of LIBOR Loans is not made on any date specified in a notice of prepayment given by the Department; (d) if all or a portion of the Taxable Loan made by an Additional Lender is designated as a LIBOR Loan or LIBOR Loans after the Interest Determination Date(s) for such LIBOR Loan(s); or (e) as a consequence of (i) any other default by the Department to repay its LIBOR Loans when required by the terms of this Agreement or the Taxable Bond of such Lender or (ii) any action taken pursuant to Section 2.9(b)

2.11. Pledge of Collateral.

(a) The Department hereby pledges, places a lien upon and assigns the Water Code Collateral, and grants a continuing security interest in all currently existing and hereafter acquired or arising Water Code Collateral, to the Lenders and the holders of the Parity Debt in order to secure the prompt payment of the principal of and interest on the Bonds, the Loans evidenced thereby and the Parity Debt as the same shall become due and payable and the prompt performance by the State and the Department of each of its covenants and duties under this Agreement, the Bonds and any other agreement, instrument or document evidencing the Parity Debt. The pledge and lien of this Agreement shall immediately attach to the Water Code Collateral without the need for any physical delivery, recordation, filing, or further act, and shall be effective, binding and enforceable against the State, the Department and all others having claims of any kind in tort, contract or otherwise against the State, the Department or the Water Code Collateral and irrespective of whether those parties have notice of such pledge and lien. The Lenders and holders of any Parity Debt shall share *pari passu* without priority or distinction of one over the other in the Water Code Collateral.

(b) The Department hereby pledges, places a lien upon and assigns the Capitalized Interest and Fees Amount, and grants a continuing security interest in Capitalized Interest and Fees Amount, to the Lenders in order to secure the prompt payment of the principal of and interest on the Bonds and the Loans evidenced thereby as the same shall become due and payable and the prompt performance by the State and the Department of each of its covenants and duties under this Agreement and the Bonds. The pledge and lien of this Agreement shall immediately attach to the Capitalized Interest and Fees Amount without the need for any physical delivery, recordation, filing, or further act, and be effective, binding and enforceable against the Department and all others having claims of any kind in tort, contract or otherwise against the Department or the Water Code Collateral and irrespective of whether those parties have notice of such pledge and lien. The Interest and Fees Account constitutes a trust fund for the security and payment of the interest on and principal of the Bonds, and the Lenders shall share *pari passu* without priority or distinction of one over the other in the Interest and Fees Account. The pledge and lien created by this Section 2.11(b) shall be prior to the claims and interests of all other Persons, including, without limitation, State Reimbursement Claims.

(c) The Department hereby authorizes and instructs the Agent to establish an interest-bearing bank account in the name of, and under the dominion and control of, the Agent as agent for the Lenders (the "Interest and Fees Account"). The Agent shall deposit all Capitalized Interest and Fees Amounts into the Interest and Fees Account. The Agent shall invest all amounts from time to time on deposit in the Interest and Fees Account in money market funds with a maturity of seven days or less. All investments made from amounts on deposit in the Interest and Fees Account and all earnings thereon shall be credited to the Interest and Fees Account. Amounts on deposit in the Interest and Fees Account shall be applied in the manner set forth in Sections 3.3(b) and 3.7. The Agent shall close the Interest and Fees Account as soon as the balance therein is zero. Neither the Agent nor any Agent-Related Person shall have any liability for any investment loss with respect to any investment made in accordance with this Section 2.11(c).

2.12. Limited Recourse. THE OBLIGATIONS ARE LIMITED OBLIGATIONS OF THE DEPARTMENT PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL. THE OBLIGATIONS ARE NOT A GENERAL OBLIGATION OF THE STATE, THE DEPARTMENT OR THE GENERAL FUND. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OR THE DEPARTMENT IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS.

SECTION 3. FEES, PREPAYMENTS AND PAYMENTS.

3.1. Fees.

(a) The Department agrees to pay to the Agent for distribution to each Lender on or prior to the Closing Date a non-refundable upfront fee equal to the product of such Lender's Commitment and 0.00125.

(b) The Department agrees to pay to the Agent for distribution to each Lender on or prior to the Closing Date a non-refundable administrative fee equal to $200,000 per Lender.

(c) So long as Loans remain outstanding on the Term Out Period Commencement Date, the Department agrees to pay to the Agent for distribution to each Lender on the Term Out Period Commencement Date a non-refundable term loan fee equal to the product of the aggregate unpaid principal balance of such Lender's Loans on such date and 0.00125.

(d) The Department shall pay to the Agent, for its own account and the account of the Lead Arranger, such fees at such times as may be agreed to from time to time in one or more letter agreements among the Department, the Agent and the Lead Arranger.

3.2. Voluntary Prepayments. The Department shall have the right to prepay the Loans, without premium or penalty, in whole or in part from time to time on the following terms and conditions:

(a) The Department shall give the Agent at its Notice Office at least five (5) Business Days' prior written notice of its intent to prepay the Loans, the amount of such prepayment, which notice the Agent shall promptly transmit to each Lender;

(b) Unless the Loans are being prepaid in full, each prepayment shall be in an aggregate principal amount of at least $50,000,000 and $5,000,000 multiples in excess thereof; and

(c) Each prepayment of Loans made pursuant to this Section 3.2 shall be applied *pro rata* among the Loans of all Lenders, irrespective of whether the Loans of such Lenders are Taxable Loans or Tax-Exempt Loans or both.

3.3. Mandatory Prepayment.

(a) In the event the Department issues or incurs any Water Code Bonds or incurs or permits to exist any other Debt payable from or secured by the Water Code Collateral other than Permitted Debt, the Department shall apply all of the proceeds of such Water Code Bonds or other Debt, net of customary and reasonable costs of issuance or incurrence and reasonable debt service reserves, to the prepayment of the Loans on the date such proceeds are received by the Department. The Department shall give the Agent at its Notice Office telephonic notice of its intent to prepay the Loans pursuant to this Section 3.3(a), the amount of such prepayment, which notice the Agent shall promptly transmit to each Lender.

(b) In the event (i) there is a positive balance in the Interest and Fees Account on March 1, 2002 and (ii) a Default, Event of Default, Noncompliance or Event of Noncompliance has occurred and is continuing on March 1, 2002, such positive balance shall be applied by the Agent to the prepayment of the Loans on March 1, 2002.

(c) Each prepayment of Loans made pursuant to this Section 3.3 shall be applied *pro rata* among the Loans of all Lenders, irrespective of whether the Loans of such Lender are Taxable Loans or Tax-Exempt Loans or both.

3.4. Principal Repayments. The Loans shall be paid in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Loans shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Loans in part, each remaining principal payment shall be reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

3.5. Method and Place of Payment. Except as otherwise specifically provided herein (including, without limitation, Section 3.7), all payments under this Agreement or any Bond shall be made to the Agent for the account of the Lender or Lenders entitled thereto not later than 2:00 p.m. on the date when due and shall be made in Dollars in immediately available funds at the Payment Account of the Agent. Whenever any payment to be made hereunder or under any Bond

shall be stated to be due on a day which is not a Business Day, the due date thereof shall be extended to the next succeeding Business Day and, with respect to payments of principal, interest shall be payable at the applicable rate during such extension.

3.6. Net Payments. All payments made by the Department hereunder or under any Bond will be made without setoff, counterclaim or other defense. All such payments will be made free and clear of, and without deduction or withholding for, any present or future taxes, levies, imposts, duties, fees, assessments or other charges of whatever nature now or hereafter imposed by any jurisdiction or by any political subdivision or taxing authority thereof or therein (but excluding, except as provided below, any tax imposed on or measured by the net income of a Lender pursuant to the laws of the jurisdiction (or any political subdivision or taxing authority thereof or therein) in which the principal office or Lending Office of such Lender is located) and all interest, penalties or similar liabilities with respect thereto (collectively, "Taxes"). The Department shall also reimburse each Lender, upon the written request of such Lender, for taxes imposed on or measured by the net income of such Lender pursuant to the laws of the jurisdiction (or any political subdivision or taxing authority thereof or therein) in which the principal office or Lending Office of such Lender is located as such Lender shall determine are payable by such Lender in respect of amounts paid to or on behalf of such Lender pursuant to the preceding sentence and/or this sentence (collectively, "Additional Taxes"). If any Taxes or Additional Taxes are so levied or imposed, the Department agrees to pay the full amount of such Taxes and Additional Taxes as may be necessary so that every payment of all amounts due hereunder or under any Bond, after withholding or deduction for or on account of any Taxes and Additional Taxes, will not be less than the amount provided for herein or in such Bond. The Department will furnish to the Agent within forty-five (45) days after the date the payment of any Taxes or Additional Taxes is due pursuant to applicable law certified copies of tax receipts evidencing such payment by the Department. The Department will, to the extent permitted by law, indemnify and hold harmless each Lender, and reimburse such Lender upon its written request, for the amount of any Taxes and/or Additional Taxes so levied or imposed and paid by such Lender.

3.7. Capitalized Interest and Fees Amount. Amounts on deposit in the Interest and Fees Account shall be applied by the Agent to pay when due interest accruing on the Loans and the Fees payable to the Agent and the Lenders under this Agreement and the other Transaction Documents during the period commencing on the Closing Date and ending on February 28, 2002, such payments to be made by the Agent to the Lenders no later than 10:30 A.M. on the date when due. In the event there is a positive balance in the Interest and Fees Account on March 1, 2002, such positive amount shall, so long as no Default, Event of Default, Noncompliance or Event of Noncompliance has occurred and is continuing on March 1, 2002, be remitted to the Department by the Agent on March 1, 2002. In the event there is a positive balance in the Interest and Fees Account on the date on which all Obligations are paid in full, such positive amount shall be remitted to the Department by the Agent as soon as practicable.

SECTION 4. CONDITIONS PRECEDENT.

4.1. Initial Loans. The obligation of each Initial Lender to make its Loan(s) on the Closing Date (or, subject to Section 2.2(a), the following Business Day) is subject to the satisfaction of the following conditions:

(a) There shall have been delivered to the Agent for the account of (i) each Lender with a Taxable Commitment, a Taxable Bond executed by the Department with a principal amount equal to such Lender's Taxable Commitment and (ii) each Lender with a Tax-Exempt Commitment, a Tax-Exempt Bond executed by the Department with a principal amount equal to such Lender's Tax-Exempt Commitment;

(b) The Executive Order shall have been adopted and all governmental and legal proceedings and all instruments and agreements in connection with the transactions contemplated in this Agreement and the other Transaction Documents shall be satisfactory in form and substance to the Agent and the Lenders, and the Agent shall have received all information and copies of all documents and papers, including records of all governmental approvals, which the Agent or any Lender reasonably may have requested in connection therewith, such documents, papers and approvals where appropriate to be certified by proper corporate or governmental authorities and to include but not be limited to:

(i) a written determination signed by the Director of the Department authorizing the issuance of the Bonds described in Section 4.1(a) and the execution and delivery of this Agreement and the other Transaction Documents and otherwise complying with the provisions of Section 80132(a) of the Water Code (the "Initial Written Determination");

(ii) written approvals signed by the California Director of Finance and the Treasurer approving the issuance of the Bonds described in Section 4.1(a) and the execution and delivery of this Agreement and the other Transaction Documents; and

(iii) the notification of the Initial Written Determination from the California Director of Finance to the Chairperson of the Joint Legislative Budget Committee and the chairperson of the committee in each house of the Legislature that considers appropriations;

(c) The Agent shall have received an opinion, dated the Closing Date, of the Attorney General of the State, addressed to the Agent and the Lenders, addressing such matters as the Agent or the Lenders may request;

(d) The Agent shall have received an opinion, dated the Closing Date, of the Chief Counsel to the Department, addressed to the Agent and the Lenders, addressing such matters as the Agent or the Lenders may request;

(e) The Agent shall have received an opinion, dated the Closing Date, of Orrick, Herrington & Sutcliffe LLP, special counsel to the Department, addressed to the Agent and the Lenders, addressing such matters as the Agent or the Lenders may request;

(f) The Agent shall have received (i) an opinion, dated the Closing Date, of Hawkins, Delafield & Wood addressed to the Agent and the Lenders, addressing such matters as the Agent or the Lenders may request, including without limitation an opinion to the effect that interest on the Tax-Exempt Loans shall be excluded from income for Federal and California income tax purposes, and (ii) a reliance letter, dated the Closing Date, of Hawkins, Delafield & Wood

addressed to each TO Issuer (as that term is defined in Section 9.4(i)) named in any Tax-Exempt Bond issued on the Closing Date;

(g) The Agent and the Lenders shall be satisfied that a mechanism has been established to ensure that the Loans and the Bonds will be repaid on a timely basis from the Revenues and the other Collateral;

(h) The Agent and the Lenders shall have received written evidence satisfactory to them that up to $6,000,000,000 of Water Code Bonds to be issued by the Department (including those to be issued on the Closing Date) have received indicative investment grade ratings from Moody's Investors Service, Inc. and Standard and Poor's Ratings Service, and that such indicative ratings have not been revoked or withdrawn on or before the Closing Date;

(i) The Agent and the Lenders shall have received a tax certificate of the State in respect of the Tax-Exempt Loans signed by a duly authorized officer, dated the Closing Date;

(j) The Agent and the Lenders shall have received a certificate of the Department signed by the Director, stating that, other than events that have been disclosed in writing to the Lenders by or on behalf of the Department, no material adverse condition or material adverse change (including change in law, rule or regulation or lawsuit) has occurred or become known to the Department since April 3, 2001 that could, in the opinion of the Department, reasonably be expected to adversely affect the Department's ability to timely perform its obligations under the Transaction Documents;

(k) Decision 01-03-009 adopted by the CPUC on March 7, 2001 shall not have been amended or modified and shall remain in full force and effect, and if the Department and the CPUC have entered into a "rate agreement," such rate agreement shall be in form and substance reasonably satisfactory to the Lenders, shall not have been amended or modified and shall remain in full force and effect;

(l) The Agent shall be satisfied that (i) this Agreement creates in favor of the Lenders, as security for the Obligations hereunder and under the other Transaction Documents, a perfected, first priority security interest in all of the Department's right, title and interest in the Collateral contemplated by Section 2.11, subject only to the payment of Operating and Maintenance Costs as contemplated by Section 2.11; and (ii) all steps required under applicable law or requested by the Agent shall have been taken to ensure that this Agreement creates a valid, perfected, first priority security interest as contemplated by Section 2.11 on all Collateral, subject only to the payment of Operating and Maintenance Costs as contemplated by Section 2.11;

(m) The Department shall have paid to the Agent all fees due on or prior to the Closing Date in accordance with Section 3.1(a) through (d) and in accordance with the letter agreement referenced in Section 3.1(d) and all costs and expenses owing to the Agent and Agent's counsel through the Closing Date;

(n) The Agent and the Lenders shall be satisfied that (i) the representations and warranties set forth in Section 5 of this Agreement and in all the other Transaction Documents are true and correct in all material respects, and (ii) except for events that have been disclosed in writing to the Lenders by or on behalf of the Department, no material adverse condition or material adverse change (including change in law, rule or regulation or lawsuit) has occurred or

become known to the Agent or the Lenders since April 3, 2001 that could, in their opinion, reasonably be expected to adversely affect the Department's ability to timely perform its obligations under the Transaction Documents; and

(o) The Agent and Lenders shall have received such other documents, certificates, opinions, approvals and filings with respect to this Agreement and the other Transaction Documents as the Agent or Lenders may reasonably request.

All the Bonds, certificates, opinions and other documents and papers referred to in this Section 4.1, unless otherwise specified, shall be delivered to the Agent for the account of each of the Lenders and, except for the Bonds, in sufficient counterparts for the Agent and each of the Lenders and shall be satisfactory in form and substance to the Lenders.

4.2. Additional Loans. The obligation of an Additional Lender to make its Loan(s) on a Secondary Closing Date (or, subject to Section 2.2(b), the following Business Day) is subject to the satisfaction of the following conditions:

(a) There shall have been delivered to the Agent for the account of such Additional Lender (i) if it has an Additional Taxable Commitment, a Taxable Bond executed by the Department with a principal amount equal to such Lender's Additional Taxable Commitment and (ii) if it has an Additional Tax-Exempt Commitment, a Tax-Exempt Bond executed by the Department with a principal amount equal to such Lender's Additional Tax-Exempt Commitment;

(b) All governmental and legal proceedings and all instruments and agreements in connection with the transactions contemplated in this Agreement and the other Transaction Documents shall be satisfactory in form and substance to the Agent and each such Additional Lender, and the Agent shall have received all information and copies of all documents and papers, including records of all governmental approvals, which the Agent or any such Additional Lender reasonably may have requested in connection therewith, such documents, papers and approvals where appropriate to be certified by proper corporate or governmental authorities and to include but not be limited to:

(i) a written determination signed by the Director of the Department authorizing the issuance of the Bonds described in Section 4.2(a) and the reaffirming the execution and delivery of this Agreement and the other Transaction Documents and otherwise complying with the provisions of Section 80132(a) of the Water Code (each, a "Secondary Written Determination");

(ii) written approvals signed by the California Director of Finance and the Treasurer approving the issuance of the Bonds described in Section 4.2(a) and reaffirming the execution and delivery of this Agreement and the other Transaction Documents; and

(iii) the notification of the Secondary Written Determination from the California Director of Finance to the Chairperson of the Joint Legislative Budget Committee and the chairperson of the committee in each house of the Legislature that considers appropriations;

(c) The Agent shall have received an opinion, dated the applicable Secondary Closing Date, of the Attorney General of the State, addressed to the Additional Lenders, addressing such matters as the Additional Lenders may request;

(d) The Agent shall have received an opinion, dated the applicable Secondary Closing Date, of the Chief Counsel to the Department, addressed to the Agent and the Lenders, addressing such matters as the Additional Lenders may request;

(e) The Agent shall have received an opinion, dated the applicable Secondary Closing Date, of Orrick, Herrington & Sutcliffe LLP, special counsel to the Department, addressed to the Additional Lenders, addressing such matters as the Additional Lenders may request;

(f) The Additional Lenders shall have received an opinion, dated the Closing Date, of Hawkins, Delafield & Wood addressed to the Additional Lenders, addressing such matters as the Additional Lenders may request, including without limitation an opinion to the effect that interest on the Tax-Exempt Loans shall be excluded from income for Federal and California income tax purposes;

(g) The Additional Lenders shall be satisfied that a mechanism has been established to ensure that the Loans and the Bonds of such Additional Lenders will be repaid on a timely basis from the Revenues and the other Collateral;

(h) The Additional Lenders shall be satisfied that the indicative ratings letters delivered to the Agent and the Lenders pursuant to Section 4.1(h) shall not have been revoked or withdrawn on or before the applicable Secondary Closing Date;

(i) If Tax-Exempt Loans are to be issued on the applicable Secondary Closing Date to Additional Lenders, the Agent and such Additional Lenders shall have received a tax certificate of the State in respect of such Tax-Exempt Loans signed by a duly authorized officer, dated the applicable Secondary Closing Date;

(j) The Agent and Additional Lenders shall have received a certificate of the Department signed by the Director, stating that the representations and warranties set forth in Section 5 of this Agreement and in all the other Transaction Documents are true and correct in all material respects as of the applicable Secondary Closing Date, as if made on the applicable Secondary Closing Date;

(k) Decision 01-03-009 adopted by the CPUC on March 7, 2001 shall not have been amended or modified and shall remain in full force and effect, and if the Department and the CPUC have entered into a "rate agreement," such rate agreement shall be in form and substance reasonably satisfactory to the Lenders, shall not have been amended or modified and shall remain in full force and effect;

(l) The Department shall have paid to the Additional Lenders all fees and expenses due on or prior to the applicable Secondary Closing Date in accordance with any letter agreement with the Department;

(m) The Additional Lenders shall be satisfied that (i) the representations and warranties set forth in Section 5 of this Agreement and in all the other Transaction Documents are true and

correct in all material respects as of the applicable Secondary Closing Date as if made on the applicable Secondary Closing Date, and (ii) except for events that have been disclosed in writing to the Additional Lenders by or on behalf of the Department, no material adverse condition or material adverse change (including change in law, rule or regulation or lawsuit) has occurred or become known to the Additional Lenders since the date of this Agreement that could, in their opinion, reasonably be expected to adversely affect the Department's ability to timely perform its obligations under the Transaction Documents; and

(n) The Additional Lenders shall have received such other documents, certificates, opinions, approvals and filings with respect to this Agreement and the other Transaction Documents as the Additional Lenders may reasonably request.

All the Bonds, certificates, opinions and other documents and papers referred to in this Section 4.2, unless otherwise specified, shall be delivered to the Agent for the account of each of the Additional Lenders and, except for the Bonds, in sufficient counterparts for the Agent and each of the Additional Lenders and shall be satisfactory in form and substance to the Additional Lenders.

SECTION 5. REPRESENTATIONS, WARRANTIES AND AGREEMENTS.

In order to induce the Agent and each of the Lenders to enter into this Agreement and to make the Loans, the Department makes the following representations, warranties and agreements as of the date of this Agreement and as of the Closing Date, which shall survive the execution and delivery of this Agreement and the Bonds and the making of the Loans:

5.1. Power and Authority. The Department has all requisite power and authority to adopt, issue, execute, deliver and perform all of its obligations under this Agreement and the other Transaction Documents and to incur the Obligations, and to adopt, issue, execute and deliver any and all instruments and documents required to be adopted, executed or delivered pursuant to or in connection herewith or therewith and to perform each and all of the matters and things provided for herein and therein.

5.2. No Violation. The execution, delivery and performance by the Department of this Agreement and the other Transaction Documents and any and all instruments or documents required to be adopted, issued, executed or delivered in connection herewith or therewith have been duly authorized and do not and will not (i) violate any provision of the Constitution of the State or the U.S., any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award in effect having applicability to the State or the Department or (ii) result in a breach of or constitute a default under any indenture, loan, credit agreement or any other agreement, lease or instrument to which the State or the Department is a party or by which the State or the Department is bound which could reasonably be expected to adversely affect the State's or the Department's ability to satisfy and perform its obligations under the Transaction Documents.

5.3. Authorization. No authorization, order, consent, approval, license, exemption from or registration with any Governmental Authority, other than those which have been obtained, is necessary for the valid adoption, issuance, execution, delivery and performance by the Department of any of the Transaction Documents.

5.4. Binding Agreements. This Agreement and each of the other Transaction Documents constitutes the legal, valid and binding obligation of the State, enforceable against the State in accordance with its terms, except as such enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against the State of California as referenced in California Code of Civil Procedure Sections 695.040, 695.050 and 712.070 and California Government Code Sections 900 through 985. As of the date hereof, the Department is not entitled to the benefits as a debtor under any federal or California law relating to bankruptcy, insolvency, reorganization, conservatorship or relief of debtors.

5.5. No Litigation. Except as set forth on Schedule 3, there is no action, suit, proceeding, inquiry or investigation at law or in equity before or by any arbitrator, Governmental Authority, pending with service made or, to the best knowledge of the Department, threatened against or affecting the State, the CPUC or the Department, which (a) in any manner draws into question the constitutionality, validity or enforceability of any of the Transaction Documents or the pledge of or lien over the Collateral contained herein, (b) in any way contests the existence, organization or powers of the State or the Department or any elected or appointed official thereof to adopt, execute and deliver any of the Transaction Documents or perform the obligations thereunder or contemplated thereby, (c) in any way contests the constitutionality or validity of AB1X, Division 27 of the Water Code, the Emergency Proclamation, the Executive Order or the powers of the State or the Department thereunder, including without limitation the power of the Department to purchase and sell electric power and collect payment for such electric power or to establish a revenue requirement, or the Emergency Services Act or (d) could reasonably be expected to have a Material Adverse Effect.

5.6. Sovereign Immunity. The State is not entitled to any immunity from any legal proceedings to enforce this Agreement or any other Transaction Document (including, without limitation, immunity from service of process of any court otherwise having jurisdiction).

5.7. Compliance. The Department is in compliance with the terms and conditions of this Agreement and each of the other Transaction Documents, and no breach of the terms hereof or thereof nor any Default, Event of Default, Noncompliance or Event of Noncompliance has occurred and is continuing or could reasonably be expected to result from the making of the Loans.

5.8. First Priority Lien. Section 2.11 of this Agreement is sufficient, without further action on the part of the Agent, the Lenders, the State, the Department or any other Person, to create in favor of the Lender a valid and enforceable security interest in all right, title and interest of the Department in the Collateral, and the Lenders have a fully perfected, first priority lien on, and security interest in, all right, title and interest of the Department in all of the Collateral, subject to no other Liens, including, without limitation, the State Reimbursement Claims, provided that the Department may first apply the Water Code Collateral to the payment of Operation and Maintenance Costs as the same are due.

5.9. True and Complete Disclosure.

(a) All information other than projections (the "Information") that has been or will be made available to the Agent or any Lender by or on behalf of the Department is or will be, when furnished, correct in all material respects as of its date and does not or will not, when furnished, contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements contained therein not materially misleading in light of the circumstances under which such statements are made, except to the extent such Information has been superseded by Information that is correct in all material respects as of its date and does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements contained therein not materially misleading in the light of the circumstances under which such statements are made.

(b) All projections that have been or will be made available to the Agent or any Lender by or on behalf of the Department have been or will be prepared in good faith based upon reasonable assumptions.

5.10. Compliance with Statutes. The Department is in compliance with all provisions of AB1X and the Executive Order. The Department is in compliance with all other applicable statutes, regulations and orders of, and all applicable restrictions imposed by, all Governmental Authorities, in respect of the conduct of its operations, the ownership of its property and the performance of its duties and obligations except for such non-compliances which, individually or in the aggregate, could not result in a Material Adverse Effect.

5.11. Use of Proceeds; Margin Regulations. Neither the making of any Loan nor the use of the proceeds thereof will violate or be inconsistent with the provisions of Regulation U of the Board of Governors of the Federal Reserve System.

SECTION 6. COVENANTS.

The Department covenants and agrees that on and after the Closing Date and until the Loans and the Bonds, together with interest, and all other obligations incurred hereunder and under the other Transaction Agreements, are paid in full:

6.1. Information Covenants. The Department will furnish to the Agent and each Lender:

(a) Budgets. Within thirty days of adoption, any budget (including budgeted statements of Revenues, and sources and uses of cash and balance sheets) or any amendment or modification thereof prepared by or on behalf of the Department for the Electric Power Fund accompanied by a statement of the chief financial officer of the Department to the effect that, to the best of his or her knowledge, such budget is a reasonable estimate for the period covered thereby.

(b) Notice of Default or Litigation. As soon as practicable, and in any event within ten days after the Chief Counsel of the Department or an Authorized Officer obtains knowledge thereof, notice of (i) the occurrence of any event or circumstance which constitutes a Default, Event of Default, Noncompliance or Event of Noncompliance or (ii) any litigation or

governmental proceeding pending against the State or the Department which could reasonably be expected to have a Material Adverse Effect.

(c) Term Out Period Information. Not later than the twentieth day of each calendar month, beginning on November 20, 2001, (i) a statement in form and substance reasonably acceptable to the Agent identifying components comprising the Revenues for the preceding calendar month and the amounts thereof, (ii) a balance sheet for the Electric Power Fund as at the end of the preceding calendar month and related statement of operations for such Fund, (iii) a statement identifying cash deposits to and payments from the Electric Power Fund during the preceding calendar month and (iv) a certificate, with supporting calculations, demonstrating compliance by the Department with Section 6.8.

(d) Revenue Requirement. As soon as practicable, and in any event within five Business Days, a copy of each revenue requirement under Division 27 of the Water Code and the Executive Order that is conveyed by the Department to the CPUC.(

(e) CPUC. As soon as practicable, and in any event within five Business Days, a copy of all written communications between the Department and the CPUC and a copy of all actions (including, without limitation, orders) taken by the CPUC, in each case with respect to matters governed by Division 27 of the Water Code and/or the Executive Order. Promptly, and in any event within two Business Days after an officer of the Department or the State obtains knowledge thereof, notice of any order or decree of a court of competent jurisdiction staying or enjoining action (including, without limitation, orders) taken by the CPUC with respect to matters governed by Division 27 of the Water Code and/or the Executive Order.

(f) Power Supply Agreements. As soon as practicable, and in any event within ten Business Days of execution, a copy of each significant power supply agreement entered into by the Department pursuant to Division 27 of the Water Code and/or the Executive Order.

(g) Projections. No later than the first Business Day of each calendar quarter, commencing with the calendar quarter beginning on October 1, 2001, projections of the Department for such calendar quarter of (i) the Department's power purchase costs for power to be purchased pursuant to Division 27 of the Water Code and the Executive Order for such quarter, (ii) the Revenues for such quarter, (iii) Operating and Maintenance Costs for such quarter and (iv) debt service on all Water Code Bonds for such quarter, which projections shall be certified as to reasonable basis and assumptions (A) in the case of clause (i) by an Independent Consultant and (B) in all cases by an Authorized Representative.

(h) Legislation. As soon as practicable, and in any event within five Business Days after the Chief Counsel of the Department or an Authorized Officer obtains knowledge thereof, a copy of any assembly bill adopted by the assembly, senate bill adopted by the senate, voter initiative qualified with the Attorney General or official action on the part of the Governor which purports to amend, modify, supplement or repeal any provision of AB1X, the Emergency Proclamation, the Executive Order or the Emergency Services Act.

(i) Debt Documents. As soon as practicable, and in any event within five Business Days of execution, a copy of any agreement between the Department and any Person (other than

the State) to advance funds, loan money or extend credit to the Department in connection with the Department's power purchase program under AB1X and/or the Executive Order.

(j) Other Information. From time to time, such other information or documents (financial or otherwise) as any Lender or the Agent may reasonably request.

6.2. Books, Records and Inspections. The State will maintain adequate books, accounts and records in order to present its financial statements as required by the laws of the State. Without limiting the foregoing, the Department will keep proper books, accounts and records in respect of the Electric Power Fund and the Revenues in which full, true and correct entries in conformity with GAAP or SAP, as the case may be, and all requirements of law shall be made of all dealings and transactions in relation to its operations and activities pursuant to Division 27 of the Water Code and the Executive Order. The Department will permit officers and designated representatives of the Agent, or any Lender to examine and audit the books, accounts and records of the State and the Department and discuss the affairs, finances and accounts of the State and the Department with, and be advised as to the same by, their officers, all at such reasonable times and intervals and to such reasonable extent as the Agent or such Lender may request.

6.3. Punctual Payment. The Department shall duly and punctually pay or cause to be paid all Obligations, including without limitation the Loans and the Bonds, on the date, at the place and in the manner provided in this Agreement and the other Transaction Documents, all in strict conformity with the terms hereof and thereof, and will faithfully observe and perform all of the other obligations, conditions, covenants and requirements on its part contained herein or therein, and agrees that the time of such payment and performance is of the essence of the Department's contract with the Agent and the Lenders.

6.4. Sell Electric Power. The Department shall sell electric power to retail end use customers of the Electrical Corporations.

6.5. Discharge Claims. In order to fully preserve and protect the priority and security of the Loans, Bonds and other Obligations, the Department shall pay from the Electric Power Fund and discharge all lawful claims for purchased power, labor, materials and supplies furnished for or in connection with the affairs and activities of the Department contemplated by Division 27 of the Water Code and the Executive Order which, if unpaid, may become a Lien upon the Collateral or impair the security thereof. The Department shall also pay from the Electric Power Fund all taxes and assessments or other governmental charges lawfully levied or assessed upon or in respect of the affairs and activities contemplated by Division 27 of the Water Code and the Executive Order or upon any of the Revenues.

6.6. No Lien; Non-Impairment.

(a) The Department will not permit to exist any Lien over the Revenues and the other Collateral except to secure Permitted Debt in accordance with Section 6.9, and shall not dispose of or use the Revenues or the other Collateral except as authorized or permitted by this Agreement. The Department shall not enter into any agreement, take any action or omit to take any action which could reasonably be expected to impair the ability of the Department to secure adequate Revenues to pay the Obligations or perform its other obligations under the Transaction

Documents or which otherwise could reasonably be expected to impair the Liens, rights, powers and privileges of the Agent or the Lenders purported to be created by the Transaction Documents.

(b) As authorized by Water Code Section 80200(e) and the Executive Order, the Department includes in this Agreement the following pledge of the State:

While any Bonds or Loans remain outstanding and not fully performed or discharged, the rights, powers, duties and existence of the Department and the CPUC shall not be diminished or impaired in any manner that will adversely affect the interests or rights of the Agent or any Lender.

6.7. Electric Power Fund.

(a) Revenues. All Revenues shall be promptly deposited in and credited to the Electric Power Fund.

(b) Investments. All obligations purchased by the investment of moneys in the Electric Power Fund shall be deemed at all times to be part of the Electric Power Fund and any income realized from such investments shall be credited to the Electric Power Fund. Amounts on deposit in the Electric Power Fund may only be invested in instruments and securities permitted from time to time by the State's adopted investment policy.

(c) Payments. Moneys on deposit in or credited to the Electric Power Fund shall only be expended for the following purposes and in the following order of priority:

(i) to pay Operating and Maintenance Costs when due;

(ii) to pay when due principal of and interest on the Bonds, and the Loans evidenced thereby, the Parity Debt and all other amounts payable under this Agreement and the other Transaction Documents;

(iii) to pay the principal of and interest on Permitted Debt (other than Parity Debt) when due; and

(iv) to pay any other amounts required by law to be paid from the Electric Revenue Fund;

provided that, so long as any Obligations remain outstanding or unpaid, no moneys on deposit in or credited to the Electric Power Fund and no Collateral shall be used or applied to pay State Reimbursement Claims.

6.8. Revenue Requirements. The Department shall, at least annually, and more frequently as required, establish and revise Revenue Requirements which, after taking into account any amounts on deposit in, or securities credited to, or projected from sources other than Revenues to be on deposit in, or credited to, the Electric Power Fund and the Interest and Fees Account, shall be at least sufficient to pay the amounts set forth in Section 6.7(c)(i)-(iv), and shall advise the CPUC of such Revenue Requirements. Each Revenue Requirement shall make allowances for contingencies and errors in estimates and shall be established so that the Net

Revenues at any time shall be at least 1.10 times the estimated amounts payable under Section 6.7(c)(ii) during the next three calendar months. Each Revenue Requirement shall request the CPUC to promptly set a rate or rates with respect to retail end use customers of the Electrical Corporations, measured as a function of the power sold or to be sold by the Department to or on behalf of such retail end use customers, and which rate or rates shall be separate, distinct and independent from any rate or rates of or to be established by the CPUC for any Electrical Corporation or in such other manner as will result in revenues being the property of the Department and not the property of any Electrical Corporation (a "Properly Structured Charge").

6.9. Limits on Additional Debt. No additional Debt payable out of or having a Lien on the Revenues or the Water Code Collateral shall be created or incurred other than:

(i) Parity Debt; and

(ii) Debt which is subordinated to the obligations of the Department under this Agreement and the other Transaction Documents on terms approved by all of the Initial Lenders and, if at the time such Debt is to be incurred Loans have been made pursuant to Section 2.2(b), Lenders (including all Initial Lenders) whose Pro Rata Shares in the aggregate exceed 60%, the proceeds of which are applied to the payment of Loans pursuant to Section 3.3 hereof; and

the terms of such Debt do not permit or provide for such Debt to become due (by acceleration, repurchase, redemption or otherwise) prior to its stated maturity or require or permit the holder of such Debt to require the Department to provide cash collateral in respect thereof.

6.10. Rate Agreement. As soon as practicable following the Closing Date, but not later than September 30, 2001 (or October 10, 2001, if urgency legislation of the Legislature becomes effective prior to September 30, 2001 and establishes that the period for filing an application for rehearing of a CPUC Order regarding the effectiveness of the Rate Agreement is ten days), the Department and the CPUC shall execute and deliver the Rate Agreement which, among other things, shall request the CPUC to establish Properly Structured Charges upon delivery of Revenue Requirements.

6.11. Servicing.

(a) With respect to each Electrical Corporation, as soon as practicable following the Closing Date, but not later than September 30, 2001 (or October 10, 2001, if urgency legislation of the Legislature becomes effective prior to September 30, 2001 and establishes that the period for filing an application for rehearing of a CPUC Order regarding the effectiveness of a Servicing Agreement or a Servicing Order is ten days), the Department shall have either (i) caused the CPUC to issue a Servicing Order applicable to such Electrical Corporation or (ii) entered into a Servicing Agreement with such Electrical Corporation.

(b) To the extent an Electrical Corporation has entered into a Servicing Agreement with the Department, the Department shall use its best efforts to cause such Electrical Corporation to comply with the terms of such Servicing Agreement. To the extent an Electrical Corporation has not entered into a Servicing Agreement with the Department but the CPUC has issued a Servicing Order which applies to such Electrical Corporation, the Department shall use

its best efforts to cause such Electrical Corporation to comply with the terms of such Servicing Order.

(c) Whether or not a Servicing Order has been issued by the CPUC with respect to an Electrical Corporation or an Electrical Corporation has entered into a Servicing Agreement with the Department, in the event such Electrical Corporation fails to bill, collect, segregate and remit Revenues to or on behalf of the Department, the Department shall use its best efforts to promptly and diligently enforce and prosecute its rights under AB1X, the Executive Order, any such Servicing Order or any such Servicing Agreement.

6.12. Related Documents. The Department shall not terminate, or agree to amend or modify any Servicing Agreement or the Rate Agreement once the same have been executed and delivered, if as a result thereof, the Department's ability to pay and perform its obligations under this Agreement and the other Transaction Documents could reasonably be expected to be materially impaired.

6.13. Customer Access. The Department shall use its best efforts to cause the CPUC, pursuant to Section 80110 of the Water Code and the Executive Order, on or prior to October 31, 2001, to set a date beginning on which the right of retail end use customers to purchase electrical power from providers other than the Department and Electrical Corporations shall be suspended, which date shall not be later than November 30, 2001, unless, on or before October 31, 2001, the Legislature has enacted legislation in form and substance satisfactory to the Majority Lenders which suspends, or otherwise governs and controls, such right in a manner which protects the Department from any material decrease in Revenues from the exercise of such rights.

6.14. Tax Covenants. Notwithstanding any other provision of this Agreement, absent an opinion of Bond Counsel that the exclusion from gross income of interest on the Tax-Exempt Bonds or Tax-Exempt Loans will not be adversely affected for federal income tax purposes, the Department covenants to comply with all applicable requirements of the Code necessary to preserve such exclusion from gross income and specifically covenants, without limiting the generality of the foregoing, as follows:

(a) Private Activity. The Department will not take or omit to take any action or make any use of the proceeds of the Tax-Exempt Bonds or Tax-Exempt Loans or of any other moneys or property which would cause the Tax-Exempt Bonds or Tax-Exempt Loans to be "private activity bonds" within the meaning of Section 141 of the Code.

(b) Arbitrage. The Department will make no use of the proceeds of the Tax-Exempt Bonds or Tax-Exempt Loans or of any other amounts or property, regardless of the source, or take or omit to take any action which would cause the Tax-Exempt Bonds or Tax-Exempt Loans to be "arbitrage bonds" within the meaning of Section 148 of the Code.

(c) Federal Guarantee. The Department will make no use of the proceeds of the Tax-Exempt Bonds or Tax-Exempt Loans or take or omit to take any action that would cause the Tax-Exempt Bonds or Tax-Exempt Loans to be "federally guaranteed" within the meaning of Section 149(b) of the Code.

(d) Information Reporting. The Department will take or cause to be taken all necessary action to comply with the informational reporting requirements of Section 149(e) of the Code.

(e) Miscellaneous. The Department will take no action inconsistent with its expectations stated in any tax certificate executed with respect to the Tax-Exempt Bonds or Tax-Exempt Loans and will comply with the covenants and requirements stated therein and incorporated by reference herein.

This Section and the covenants set forth herein shall not be applicable to, and nothing contained herein shall be deemed to prevent the Department from issuing, Bonds or Loans the interest on which has been determined by Bond Counsel to be subject to federal income taxation.

6.15. Use of Proceeds. The proceeds of the Loans shall be used by the Department solely for the purposes authorized by clauses (1) through (3) (inclusive) of Section 80200(b) of the Water Code and the Executive Order, as in effect on the date hereof. No proceeds of the Loans shall be used by the Department to pay State Reimbursement Claims.

6.16. "Most Favored Nations" Treatment.

(a) The Department agrees (i) to disclose to the Lenders all agreements (including, without limitation, letter agreements, short-form agreements and long-form agreements) now or hereafter in effect with any Person that has loaned or advanced money or extended credit to the Department secured against the Revenues, or which proposes to do any of the foregoing, and (ii) to take such further action and/or execute such further documents (including any amendment or supplement to this Agreement) as may, in the reasonable judgment of the Majority Lenders, be necessary or desirable in order to grant to the Lenders the benefit of any more favorable terms granted to any such other Person pursuant to any such agreement.

(b) Each Initial Lender shall be entitled to receive the same treatment as any Lender which is similarly situated but not an Initial Lender with respect to fees, interest rates, discounts or other similar terms and conditions hereunder.

6.17. Waiver of Sovereign Immunity. The Department agrees that it will not assert any immunity it may have as a state agency against lawsuits brought under this Agreement or any Bond or in connection therewith that are filed in any California court or any U.S. court located in the Northern or Eastern District of California.

6.18. Further Assurances. The Department will execute any and all further documents, financing statements, agreements and instruments, and take all further action that the Majority Lenders or the Agent may reasonably request in order to effectuate the transactions contemplated by the Transaction Documents and in order to grant, preserve, protect and perfect the validity and first priority of the security interests created or intended to be created pursuant to Section 2.11 hereof.

SECTION 7. EVENTS OF DEFAULT; EVENTS OF NONCOMPLIANCE.

7.1. Events of Default. The occurrence or existence of any of the following specified events shall each constitute an "Event of Default":

(a) The Department shall (i) default in the payment when due of any principal of any Loan or any Bond or (ii) default, and such default shall continue unremedied for two or more Business Days, in the payment when due of any interest on any Loan or any Bond or any fees or any other amounts owing hereunder or under any Transaction Document; or

(b) Any representation, warranty or statement made by or on behalf of the Department herein or in any other Transaction Document or in any certificate delivered pursuant hereto or thereto shall prove to be untrue in any material respect on the date as of which made or deemed made; or

(c) The Department shall (i) default in the due performance or observance by it of any term, covenant or agreement contained in Section 6.1(b), 6.4, 6.6, 6.7, 6.8, 6.9, 6.10, 6.11(c), 6.12, 6.14 or 6.15; or (ii) default in the due performance or observance by it of any term, covenant or agreement contained in Section 6.1 (other than 6.1(b)), 6.2, 6.3 (to the extent not included within Section 7.1(a)), 6.5 and 6.16 and such default shall continue unremedied for a period of thirty days from the occurrence of such default; or

(d) The Department shall (i) default in any payment of any Permitted Debt or Parity Debt beyond the period of grace (not to exceed five days), if any, provided in the instrument or agreement under which such Debt was created or (ii) default in the observance or performance of any agreement or condition relating to any Permitted Debt or Parity Debt or contained in any instrument or agreement evidencing, guaranteeing, securing or relating to any such Debt, or any other event shall occur or condition exist, the effect of which default or other event or condition is to cause, or to permit the holder or holders of such Debt (or a trustee or agent on behalf of such holder or holders) to cause (determined without regard to whether any notice is required), such Debt to become due (whether by acceleration, repurchase, redemption or otherwise) prior to its stated maturity or cash collateral in respect thereof to be demanded, or any Permitted Debt or Parity Debt shall be declared to be due and payable, or required to be prepaid other than by a regularly scheduled required prepayment, prior to the stated maturity thereof; or

(e) If the Department has entered into a Rate Agreement, the Department or any Person acting by or on behalf of the Department shall attempt to deny or disaffirm the Department's obligations under such Rate Agreement; or

(f) If the Department has entered into a Servicing Agreement with an Electrical Corporation, the Department or any Person acting by or on behalf of the Department shall attempt to deny or disaffirm the Department's obligations under such Servicing Agreement; or

(g) The Department or any Person acting by or on behalf of the Department shall attempt to deny or disaffirm the Department's obligations under this Agreement, the other Transaction Documents, AB1X, Division 27 of the Water Code or the Executive Order or shall contest the validity or enforceability thereof; or

(h) The State shall default in the due performance or observance by it of its obligation set forth in Section 6.6(b).

7.2. Events of Noncompliance. The occurrence or existence of any of the following specified events shall each constitute an "Event of Noncompliance":

(a) The Department shall default in the due performance or observance by it of any term, covenant or agreement (other than those referred to in clauses (a), (b) and (c) of Section 7.1) contained in this Agreement or any other Transaction Document and such default shall continue unremedied for a period of ten days after the occurrence of such default; or

(b) If a Servicing Order has been issued by the CPUC with respect to one or more Electrical Corporations, such Servicing Order shall (i) no longer be in full force and effect, unless such Servicing Order has been replaced with another Servicing Order which is in form and substance satisfactory to the Agent and the Majority Lenders, (ii) be suspended or stayed by any court, the CPUC or other Governmental Authority, (iii) be declared to be unconstitutional or null and void by any court of competent jurisdiction in a final non-appealable judgment, or (iv) be modified or amended in such a manner as could reasonably be expected to have a Material Adverse Effect, unless in any such case there shall be in effect a Servicing Agreement with each Electrical Corporation that is or was bound by such Servicing Order; or

(c) If a Servicing Agreement has been entered into with an Electrical Corporation, such Servicing Agreement shall cease to be in full force and effect, unless in such case there shall be in effect a Servicing Order applicable to such Electrical Corporation; or

(d) If a Rate Agreement has been entered into between the Department and the CPUC, such Rate Agreement or any provision thereof shall cease to be in full force; or

(e) Any of this Agreement, the other Transaction Documents, AB1X, Division 27 of the Water Code, the Executive Order or any provision thereof which is material to the performance of the Department's obligations under this Agreement and the other Transactions Documents or the remedies of the Agent and the Lenders under this Agreement and the other Transactions Documents shall cease to be in full force and effect, or shall be declared to be unconstitutional, unenforceable or null and void by any court of competent jurisdiction in a final, non-appealable judgment, or shall cease to give the Agent and the Lenders the Liens, rights, powers and privileges purported to be created thereby.

(f) If the State or any department or agency thereof (i) sells electrical power to retail end use customers of the Electrical Corporations other than in accordance with Division 27 of the Water Code and/or the Executive Order or (ii) purchases electrical power for such purpose from borrowed money payable other than in accordance with Division 27 of the Water Code and/or the Executive Order.

7.3. Remedies. If any Event of Default or Event of Noncompliance shall have occurred and then be continuing, the Agent may with the consent, and shall upon the written request, of the Majority Lenders, exercise any and all of the rights and remedies available to the Agent and the Lenders under the Transaction Documents, at law or equity (including, without limitation, the

right to seek a writ of mandamus); provided that the foregoing is without prejudice to the rights of the Agent, any Lender or any Owner to enforce its claims directly against the Department.

SECTION 8. THE AGENT.

8.1. Appointment. Each Lender hereby designates and appoints Morgan Guaranty Trust Company of New York as Agent to act as specified herein and in the other Transaction Documents. Each Lender hereby irrevocably authorizes, and each Owner by the acceptance of such Bond shall be deemed irrevocably to authorize, the Agent to take such action on its behalf under the provisions of this Agreement, the other Transaction Documents and any other instruments and agreements referred to herein or therein and to exercise such powers and to perform such duties hereunder and thereunder as are specifically delegated to or required of the Agent by the terms hereof and thereof and such other powers as are reasonably incidental thereto. The Agent may perform any of its duties hereunder by or through its Affiliates or its or their officers, directors, agents or employees.

8.2. Nature of Duties. The Agent shall have no duties or responsibilities except those expressly set forth in this Agreement and the Transaction Documents. No Agent-Related Person shall be liable for any action taken or omitted by it hereunder or under any other Transaction Document or in connection herewith or therewith, unless caused by its gross negligence or willful misconduct. The duties of the Agent shall be mechanical and administrative in nature; no Agent-Related Person shall have by reason of this Agreement or any other Transaction Document a fiduciary relationship in respect of any Lender or any Owner; and nothing in this Agreement or any other Transaction Document, expressed or implied, is intended to or shall be so construed as to impose upon any Agent-Related Person any obligations in respect of this Agreement or any other Transaction Document except as expressly set forth herein.

8.3. Lack of Reliance on the Agent. Independently and without reliance upon the Agent or any other Agent-Related Person, each Lender and each Owner (as evidenced by its acceptance of a Bond), to the extent it deems appropriate, has made and shall continue to make (a) its own independent investigation of the financial condition and affairs of the Department in connection with the making and the continuance of the Loans and the taking or not taking of any action in connection herewith and (b) its own appraisal of the creditworthiness of the Department. No Agent-Related Person shall have any duty or responsibility, either initially or on a continuing basis, to provide any Lender or any Owner with any credit or other information with respect thereto, whether coming into its possession before the making of the Loans or at any time or times thereafter. No Agent-Related Person shall be responsible to any Lender or any Owner for any recitals, statements, information, representations or warranties herein or in any document, certificate or other writing delivered in connection herewith or for the execution, effectiveness, genuineness, validity, enforceability, perfection, collectibility, priority or sufficiency of this Agreement or any other Transaction Document or the financial condition of the Department or be required to make any inquiry concerning either the performance or observance of any of the terms, provisions or conditions of this Agreement or any other Transaction Document, or the financial condition of the Department or the existence or possible existence of any Default, Event of Default, Noncompliance or Event of Noncompliance.

8.4. Certain Rights of the Agent. If the Agent shall request instructions from the Majority Lenders or the Super Majority Lenders with respect to any act or action (including

failure to act) in connection with this Agreement or any other Transaction Document, the Agent shall be entitled to refrain from such act or taking such action unless and until the Agent shall have received instructions from the Majority Lenders or the Super Majority Lenders, as the case may be, and the Agent shall not incur liability to any Person by reason of so refraining or acting. Without limiting the foregoing, neither the Agent nor any Lender nor any Owner shall have any right of action whatsoever against the Agent as a result of the Agent acting or refraining from acting hereunder or under any other Transaction Document in accordance with the instructions of the Majority Lenders or the Super Majority Lenders, as the case may be.

8.5. Reliance. The Agent shall be entitled to rely, and shall be fully protected in relying, upon any note, writing, resolution, notice, statement, certificate, telex, teletype or telecopier message, cablegram, radiogram, order or other document or telephone message signed, sent or made by any Person that the Agent believed to be the proper Person, and, with respect to all legal matters pertaining to this Agreement and any other Transaction Document and its duties hereunder and thereunder, upon advice of counsel selected by it.

8.6. Indemnification. To the extent the Agent is not reimbursed and indemnified by the Department, and without limiting the Obligations, the Lenders will reimburse and indemnify each Agent-Related Person, in proportion to their respective Commitments if the Loans have not yet been made available and otherwise in proportion to their respective Loans, for and against any and all liabilities, obligations, losses, damages, penalties, claims, actions, judgments, suits, costs, expenses or disbursements of whatsoever kind or nature which may be imposed on, asserted against or incurred by the Agent in performing its duties hereunder or under any other Transaction Document, or in any way relating to or arising out of this Agreement or any other Transaction Document; provided, however, that no Lender shall be liable to any Agent-Related Person for any portion of such liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements resulting from such Agent-Related Person's gross negligence or willful misconduct.

8.7. The Agent in its Individual Capacity. With respect to its obligation to make Loans under this Agreement, the Agent shall have the rights and powers specified herein for a "Lender" and may exercise the same rights and powers as though it were not performing the duties specified herein; and the term "Lenders," "Majority Lenders," "Super Majority Lenders," "Owners" or any similar terms shall, unless the context clearly otherwise indicates, include the Agent in its individual capacity. The Agent may accept deposits from, lend money to, and generally engage in any kind of banking, trust or other business with the Department or any Affiliate of the Department as if it were not performing the duties specified herein, and may accept fees and other consideration from the Department for services in connection with this Agreement and otherwise without having to account for the same to the Lenders.

8.8. Holders. The Agent may deem and treat the Owner of any Bond as the owner thereof for all purposes hereof unless and until a written notice of the assignment, transfer or endorsement thereof or the assignment of any rights therein, as the case may be, shall have been filed with the Department and the Agent. Any request, authority or consent of any Person who, at the time of making such request or giving such authority or consent, is the Owner of any Bond or an assignee of rights therein and of which the Agent has received written notice shall be conclusive and binding on any subsequent holder, transferee, assignee or endorsee, as the case may be, of such Bond or of any Bond or Bonds issued in exchange therefor. The Department

agrees to give the Agent notice of all assignments, transfers and endorsements relating to any Bond that is filed with the Department.

8.9. Resignation by the Agent.

(a) The Agent may resign from the performance of all its functions and duties hereunder and/or under the other Transaction Documents at any time by giving forty-five days prior written notice to the Department and the Lenders. Such resignation shall take effect upon the appointment of a successor Agent pursuant to clauses (b) and (c) below or as otherwise provided below.

(b) Upon any such notice of resignation, the Lenders shall appoint a successor Agent hereunder or thereunder who shall be a commercial bank or trust company reasonably acceptable to the Department.

(c) If a successor Agent shall not have been so appointed within such 45 day period, the Agent, with the consent of the Department, may then appoint a successor Agent who shall serve as Agent hereunder or thereunder until such time, if any, as the Lenders appoint a successor Agent as provided above.

(d) If no successor Agent has been appointed pursuant to clause (b) or (c) above by the forty sixth day after the date such notice of resignation was given by the Agent, the Agent's resignation shall become effective and the Lenders shall thereafter perform all the duties of the Agent hereunder and/or under any other Transaction Document until such time, if any, as the Lenders appoint a successor Agent as provided above.

SECTION 9. MISCELLANEOUS.

9.1. Payment of Expenses, Indemnification, etc. The Department shall:

(a) Pay all reasonable out-of-pocket costs and expenses of the Agent in connection with the preparation, execution and delivery of this Agreement and the other Transaction Documents and the documents and instruments referred to herein and therein;

(b) Pay all reasonable out-of-pocket costs and expenses of the Agent and each Lender (including, without limitation, the reasonable fees and disbursements of counsel to each Lender) in connection with (i) any amendment, waiver or consent relating to any Transaction Document and (ii) the enforcement, attempted enforcement, or preservation of any rights or remedies under this Agreement or the other Transaction Documents and the documents and instruments referred to herein and therein (including all such costs and expenses incurred during any "workout" or restructuring in respect of the Obligations and during any legal proceeding); the foregoing costs and expenses shall include all search, filing, recording, charges and fees and taxes related thereto, and other reasonable out-of-pocket expenses incurred by the Agent and, in the case of clause (ii) above, the cost of outside experts retained by the Agent or any Lender. The agreements in this subsection shall survive the repayment of all the Obligations;

(c) Pay and hold the Agent and each Lender harmless from and against all filing and recording fees required to perfect the Liens granted under this Agreement;

(d) Pay and hold the Agent and each Lender harmless from and against any and all present and future stamp and other similar taxes with respect to the foregoing matters and save the Agent and each of the Lenders harmless from and against any and all liabilities with respect to or resulting from any delay or omission (other than to the extent attributable to the Agent or such Lender) to pay such taxes; and

(e) To the maximum extent permitted by law, indemnify the Agent, each Lender and their respective Affiliates and each of their respective officers, directors, employees, representatives and agents from and hold each of them harmless against any and all liabilities, obligations, losses, damages, penalties, claims, actions, judgments, suits, costs, expenses and disbursements incurred by any of them directly or indirectly as a result of, or arising out of, or in any way related to, or by reason of, any investigation, litigation or other proceeding (whether or not the Agent or any of the Lenders is a party thereto) related to the entering into and/or performance of this Agreement or any other Transaction Document or the proceeds of any Loans or the consummation of any transactions contemplated herein or in any other Transaction Document, including, without limitation, the reasonable fees and disbursements of counsel incurred in connection with any such investigation, litigation or other proceeding; provided, however, that the Department shall not be required to indemnify any indemnified person for any claims, damages, losses, liabilities, costs or expenses to the extent caused by the willful misconduct or gross negligence of such indemnified person.

9.2. Notices. Except as otherwise expressly provided herein, all notices and other communications provided for hereunder shall be in writing (including facsimile) and mailed, telecopied or delivered:

if to the Department, to:

Department of Water Resources
1416 Ninth Street, Room 805
Sacramento, California 95814
Attention: Chief, Division of Fiscal Services
Telephone: (916) 653-9836
Facsimile: (916) 653-8230

if to any Lender, to:

its Notice Office specified opposite its name on Schedule 2; and

if to the Agent, to:

its Notice Office;

or, as to the Department or the Agent, at such other address as shall be designated by such party in a written notice to the other parties hereto and, as to each other party (including the Lenders), at such other address (or to such other Person) as shall be designated by such party in a written notice to the Department and the Agent. All such notices and communications shall, when mailed, telecopied or sent by overnight courier, be effective when deposited in the mails, delivered to the overnight courier, as the case may be, or sent by telecopier upon telephonic confirmation by

the sending party, except that notices and communications to the Agent shall not be effective until received by the Agent.

9.3. Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and permitted assigns except that the Department may not assign its rights or obligations hereunder without the prior written consent of the Agent and the Super Majority Lenders (and any attempted assignment or transfer by the Department without such consent shall be null and void).

9.4. Assignments, Participations, Etc.

(a) Prior to the Term Out Period Commencement Date, no Lender may assign, transfer or convey to any Person other than a Lender Affiliate of such Lender all, or any ratable part of all, of the Loans and the other rights and obligations of such Lender under the Credit Documents without first obtaining the prior written consent of the Department (which consent may be withheld for any reason or for no reason) and the Agent (which consent shall not be unreasonably withheld). In addition to, and not by way of limitation of, the restrictions set forth in the preceding sentence, no Lender shall assign or sell any of its rights in its Tax-Exempt Loans or any interest in such Tax-Exempt Loans to any Person other than to a Lender Affiliate that will hold such Tax-Exempt Loans for its own account without first obtaining the prior written consent of the Department to the plan of distribution (as opposed to the identity of the specific purchasers under such plan), which consent may be withheld by the Department for any reason or no reason.

(b) During the Syndication Period, no Lender shall assign, transfer or convey to any Person all, or any ratable part of all, of the Loans and the other rights and obligations of such Lender under the Credit Documents unless such assignment, transfer or conveyance is made in accordance with the terms of the Syndication Agreement.

(c) Following the Syndication Period and subject to Section 9.4(d), any Lender may, with the written consent of the Department (at all times other than during the existence of a Default, an Event of Default, Noncompliance or Event of Noncompliance) and the Agent (which consents shall not be unreasonably withheld), at any time assign, transfer and convey to any one or more Persons (provided that no written consent of the Department or the Agent shall be required in connection with any assignment, transfer or conveyance by a Lender to a Lender Affiliate of such Lender or to another Lender) all, or any ratable part of all, of the Loans and the other rights and obligations of such Lender under the Credit Documents.

(d) Each assignment, transfer or conveyance made by a Lender pursuant to clauses (a) or (c) of this Section 9.4 shall (i) if a partial assignment to a Person other than a Lender Affiliate, be of Loans in a minimum amount of $10,000,000, (ii) if a partial assignment, be made as an assignment of a proportionate part of all the assigning Lender's rights and obligations under this Agreement and the other Credit Documents with respect to the Loans assigned, (iii) if a partial assignment to a Person other than a Lender Affiliate, result in the assigning Lender retaining Loans in a minimum amount of not less than $10,000,000, (iv) be made pursuant to a duly completed and executed Assignment and Acceptance Agreement in the form of Exhibit E ("Assignment and Acceptance Agreement"), and (v) be accompanied by a processing fee payable by the Assignee to the Agent in the amount of $3,500.

(e) From and after the date that the Agent notifies the assignor Lender that it has received (and provided its consent with respect to) an executed Assignment and Acceptance Agreement and payment of the above-referenced processing fee, (i) the Assignee thereunder shall be a party hereto and, to the extent that rights and obligations under the Credit Documents have been assigned to it pursuant to such Assignment and Acceptance Agreement, shall have the rights and obligations of a Lender under this Agreement, and (ii) the assignor Lender shall, to the extent that rights and obligations hereunder have been assigned by it pursuant to such Assignment and Acceptance Agreement, relinquish its rights and be released from its obligations under the Credit Documents.

(f) Immediately upon each Assignee's making its processing fee payment under Section 9.4(d), this Agreement shall be deemed to be amended to the extent, but only to the extent, necessary to reflect the addition of the Assignee and the resulting adjustment of the Loans arising therefrom and the Agent shall deliver to the Department and each Lender a revised Schedule 2 reflecting the Notice Office and Lending Office changes.

(g) Any Lender may at any time, without the consent of the Department or the Agent but with the consent of the Lead Arranger during the Syndication Period, sell to one or more Persons (a "Participant") participating interests in any Loans and the other interests of such Lender (the "Originator") hereunder and under the other Credit Documents; provided, however, that (i) the Originator's obligations under this Agreement shall remain unchanged, (ii) the Originator shall remain solely responsible for the performance of such obligations, (iii) the Department and the Agent shall continue to deal solely and directly with the Originator in connection with the Originator's rights and obligations under the Credit Documents, and (iv) no Lender shall transfer or grant any participating interest under which the Participant has rights to approve any amendment to, or any consent or waiver with respect to, this Agreement, except to the extent such amendment, consent or waiver would require unanimous consent of the Lenders as described in Section 9.10. In the case of any such participation, the Participant shall be entitled to the benefit of Sections 2.8, 2.10, 3.6 and 9.1 to the same extent as its Originator hereunder and may only enforce such rights through its Originator. Notwithstanding anything to the contrary contained in this Section 9.4(g), prior to the Term Out Period Commencement Date, each Lender shall, (i) prior to selling a participation interest in its Loans and rights and obligations under this Agreement and the other Credit Documents (other than its Tax-Exempt Loans), consult with the Department as to the identity of the proposed participant, and (ii) prior to selling a participation interest in its Tax-Exempt Loans, obtain the prior written consent of the Department to the plan of distribution (as opposed to the identity of the specific purchasers under such plan), which consent may be withheld by the Department for any reason or no reason.

(h) Notwithstanding any other provision in this Agreement, any Lender may at any time create a security interest in, or pledge, all or any portion of its rights under and interest in this Agreement in favor of any Federal Reserve Bank in accordance with Regulation A of the Federal Reserve Board or U.S. Treasury Regulation 31 CFR 203.14, and such Federal Reserve Bank may enforce such pledge or security interest in any manner permitted under applicable law; provided that payment made by the Department to or for the account of any Lender in respect of a Loan, shall satisfy the Department's payment obligation in respect of such Loan regardless of any encumbrance created pursuant to this Section 9.4(h).

(i) Notwithstanding the foregoing provisions of this Section 9.4, any Initial Lender with Tax-Exempt Loans (a "Tax-Exempt Lender") shall be entitled to include all or a portion of its Tax-Exempt Bonds in its tender option program (and the Department hereby consents thereto), in respect of which (a) such Tax-Exempt Lender or a Lender Affiliate thereof may form a trust or other special purpose issuer (a "TO Issuer"), (b) such Tax-Exempt Lender may act as placement agent and direct that the Tax-Exempt Bonds of such Lender be issued directly to its TO Issuer or a custodian acting on its behalf in exchange for delivery of the purchase price therefor by such TO Issuer, (c) the TO Issuer of a Tax-Exempt Lender may sell interests in the TO Issuer and/or in the Tax-Exempt Bonds held by such TO Issuer to investors, (d) the TO Issuer of a Tax-Exempt Lender may obtain a letter of credit in respect of the Tax-Exempt Bonds held by such TO Issuer or the interests therein or in such TO Issuer, and (e) upon the occurrence of certain adverse events relating to the Tax-Exempt Bonds or the tender option program of the TO Issuer (including loss or impairment of the credit support or the liquidity facility supporting the interests in the Tax-Exempt Bonds sold to investors, the occurrence of events of default in agreements with the related credit support or liquidity provider, a significant downgrade of the credit ratings of the interests in the Tax-Exempt Bonds created by the TO Issuer, loss of tax-exempt status of the Tax-Exempt Bonds, a dispute between the holder of voting control of the Tax-Exempt Bonds sold to the TO Issuer and the Majority Lenders or Super Majority Lenders, or a failed remarketing of such interests in the Tax-Exempt Bonds), the TO Issuer of a Tax-Exempt Lender, the Tax-Exempt Lender or a Lender Affiliate thereof or a successor to the Tax-Exempt Lender or such Lender Affiliate, may sell such Tax-Exempt Bonds in the secondary market without the restrictions set forth in Section 9.4(a)–(c) and 9.4(d)(iii) hereof. Transfers of interests in the Tax-Exempt Bonds of a Tax-Exempt Lender (as opposed to transfers of the Tax-Exempt Bonds themselves) or a TO Issuer will not be subject to the restrictions of this Section 9.4, but each TO Issuer will be subject to Section 9.17. In connection with any such tender option program, the holder of a Tax-Exempt Bond shall be entitled to the voting rights of the Tax-Exempt Lender with respect to such Tax-Exempt Bond, and shall be entitled, by notice to the Agent, to assign such voting rights to the letter of credit provider, which in turn shall be entitled, by notice to the Agent, to assign such voting rights to any reimbursement party or its designee, in each case separate from ownership of such Tax-Exempt Bond.

9.5. No Waiver; Remedies Cumulative. No failure or delay on the part of the Agent or any Lender or any Owner in exercising any right, power or privilege hereunder or under any other Transaction Document and no course of dealing between the Department, the Agent or any Lender or any Owner shall operate as a waiver hereof or thereof; nor shall any single or partial exercise of any right, power or privilege hereunder or under any other Transaction Document preclude any other or further exercise thereof or the exercise of any other right, power or privilege hereunder or thereunder. The rights, powers and remedies herein or in any other Transaction Document expressly provided are cumulative and not exclusive of any rights, powers or remedies which any Lender or any Owner would otherwise have at law, in equity or otherwise. No notice to or demand on the Department in any case shall entitle the Department to any other or further notice or demand in similar or other circumstances or constitute a waiver of the rights of any Lender or any Owner to any other or further action in any circumstances without notice or demand.

9.6. Payments Pro Rata.

(a) The Agent agrees that promptly after its receipt of each payment from or on behalf of the Department in respect of any Obligations of the Department hereunder, it shall distribute such payment to the Lenders pro rata based upon their respective shares, if any, of the Obligations with respect to which such payment was received.

(b) Each of the Lenders agrees that, if it should receive any amount hereunder (whether by voluntary payment, by realization upon security, by the exercise of the right of setoff or banker's lien, by counterclaim or cross action, by the enforcement of any right under the Transaction Documents, or otherwise), which is applicable to the payment of the principal of, or interest on, the Loans or any fee due hereunder, of a sum which with respect to the related sum or sums received by other Lenders is in a greater proportion than the total amount of such Obligation then owed and due to such Lender bears to the total amount of such Obligation then owed and due to all the Lenders immediately prior to such receipt, then such Lender receiving such excess payment shall purchase for cash without recourse or warranty from the other Lenders an interest in the Obligations of the Department to such Lenders in such amount as shall result in a proportional participation by all the Lenders in such amount; provided, however, that if all or any portion of such excess amount is thereafter recovered from such Lender, such purchase shall be rescinded and the purchase price restored to the extent of such recovery, but without interest.

9.7. Calculations; Computations. All computations of interest (other than interest calculated by reference to the Base Rate) and fees hereunder shall be made on the basis of a year of 360 days for the actual number of days (including the first day but excluding the last day) occurring in the period for which such interest or fees are payable. All computations of interest calculated by reference to the Base Rate shall be made on the basis of a year of 365/366 days, as the case may be, for the actual number of days (including the first day but excluding the last day) occurring in the period for which such interest is payable.

9.8. Governing Law; Submission to Jurisdiction; Venue; Waiver.

(a) **THIS AGREEMENT AND THE OTHER TRANSACTION DOCUMENTS AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER AND THEREUNDER SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.**

(b) Any and all disputes or legal actions or proceedings arising out of, under and/or pertaining to the Transaction Documents or any document related thereto shall be brought in the courts of the State of California located in the County of Sacramento or of the Courts of the United States of America for the Northern or Eastern Districts of California and, by execution and delivery of this Agreement, the parties hereto consent to and hereby accept for themselves and in respect of their property, generally and unconditionally, the jurisdiction of the aforesaid courts. To the extent permitted by law, the parties hereto hereby irrevocably waive any objection, including, without limitation, any objection to the laying of venue or based on the grounds of forum non conveniens, which they may now or hereafter have to the bringing of any such action or proceeding in such respective jurisdictions.

(c) The parties hereto further irrevocably consent, to the extent permitted by law, to the service of process of any of the aforementioned courts in any such action or proceeding by the mailing of copies thereof by registered or certified mail, postage prepaid, to such parties at their respective addresses pursuant to Section 9.2 hereof, such service to become effective 30 days after such mailing.

(d) **THE PARTIES HERETO WAIVE ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, SUIT, OR PROCEEDING BROUGHT TO RESOLVE ANY DISPUTE, WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE, BETWEEN ANY PARTIES ARISING OUT OF, CONNECTED WITH, RELATED TO, OR INCIDENTAL TO THE RELATIONSHIP ESTABLISHED BETWEEN THEM IN CONNECTION WITH THIS AGREEMENT OR ANY OF THE OTHER TRANSACTION DOCUMENTS OR THE TRANSACTIONS RELATED THERETO.** The scope of this waiver is intended to be all encompassing of any and all disputes that may be filed in any court and that relate to the subject matter of this transaction, including without limitation, contract claims, tort claims, breach of duty claims, and all other common law and statutory claims. The Department, the Agent and the Lenders each acknowledge that this waiver is a material inducement to enter into a business relationship, that each has already relied on the waiver in entering into this Agreement and the other Transaction Documents, and that each will continue to rely on the waiver in their related future dealings. The Department, the Agent and the Lenders further warrant and represent that each has reviewed this waiver with its legal counsel, and that each, knowingly and voluntarily waives its jury trial rights following consultation with legal counsel. **THIS WAIVER IS IRREVOCABLE, MEANING THAT IT MAY NOT BE MODIFIED EITHER ORALLY OR IN WRITING, AND THE WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS, SUPPLEMENTS OR MODIFICATIONS TO THIS AGREEMENT OR TO ANY OTHER RELATED DOCUMENT.** In the event of litigation, this Agreement may be filed as a written consent to a trial by the court.

9.9. Counterparts. This Agreement may be executed in any number of counterparts, by facsimile signatures and by the different parties hereto on separate counterparts, each of which when so executed and delivered shall be an original, but all of which shall together constitute one and the same instrument. A set of counterparts executed by all the parties hereto shall be lodged with the Department and the Agent.

9.10. Amendment or Waiver. Neither this Agreement nor any other Transaction Document nor any terms hereof or thereof may be changed, waived, discharged or terminated unless such change, waiver, discharge or termination is in writing signed by the Majority Lenders and the Agent; provided, however, that no such change, waiver, discharge or termination shall, without the consent of each Lender, (a) extend any scheduled payment date or the final maturity of any Loan or Bond, or reduce the rate or extend the time of payment of interest or fees thereon, or reduce the principal amount thereof, or increase the Commitment of any Lender over the amount thereof then in effect (it being understood that a waiver of any Default, Event of Default, Noncompliance or Event of Noncompliance not declared shall not constitute an extension, reduction or increase under this clause (a)), (b) release any Collateral except as shall be otherwise provided in any Transaction Document, (c) amend, modify or waive any provision of this Section 9.10 or Sections 2.8, 2.10, 3.3, 3.6, 6.9, 8.6, 9.1, 9.3, 9.6 or 9.7, or (d) change the percentage

specified in the definition of "Majority Lenders" or "Super Majority Lenders" or change the defined terms "Parity Debt" or "Permitted Debt."

9.11. Severability In case any provision in or obligation under this Agreement shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provisions or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

9.12. Survival. All indemnities set forth herein including, without limitation, in Sections 2.8, 2.10, 3.6, 8.6 and 9.1 shall survive the execution and delivery of this Agreement and the Notes and the making and repayment of the Loans.

9.13. Domicile of Loans. Each Lender may transfer and carry its Loans at, to or for the account of any office or Affiliate of such Lender.

9.14 Entire Agreement. This Agreement and the other Transaction Documents embody the entire agreement and understanding among the Department, the Lenders and the Agent, and supersede all prior or contemporaneous agreements and understandings of such Persons, verbal or written, relating to the subject matter hereof and thereof, except for (a) the letter agreements regarding fees referenced in Section 3.1(d), (b) the letter agreement, dated April 3, 2001, among the Department, Chase Securities, Inc. and Morgan Guaranty Trust Company of New York regarding market flex and (c) the Syndication Agreement.

9.15 Joinder of Additional Lenders. This Agreement shall become effective with respect to each Additional Lender, and each Additional Lender shall become a Lender with all of the rights and obligations attendant thereto, on the date (the "Effective Date") on which such Additional Lender shall have executed a Joinder in the form of Exhibit F hereto and shall have delivered the same to the Agent and the Department (each, a "Joinder"). The Agent will give the Department and each Lender prompt written notice of the occurrence of the Effective Date with respect to the Joinder of each Additional Lender.

9.16. Indemnification in respect of Tax-Exempt Loans. Each Tax-Exempt Lender that sells or attempts to sell Tax-Exempt Bonds, directly or indirectly through its Affiliates, shall indemnify the State, its respective departments and agencies (including the Department) and its officers, employees and agents from and hold each of them harmless against any and all liabilities, obligations, losses, damages, penalties, claims, actions, judgments, suits, costs, expenses and disbursements incurred by any of them directly or indirectly, including, without limitation, the reasonable fees and disbursements of counsel, as a result of, or arising out of, (i) the violation in connection with the sale of Tax-Exempt Bonds or interests therein of any federal or state securities laws by such Tax-Exempt Lender or any Affiliate thereof to whom such Tax-Exempt Lender has, directly or indirectly, transferred all or a portion of its Tax-Exempt Loans or (ii) any untrue statement or alleged untrue statement of any material fact contained in any information provided by such Tax-Exempt Lender or Affiliate to any purchaser of Tax-Exempt Bonds from such Tax-Exempt Lender or Affiliate or caused by any 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 as to information provided in writing by any such indemnified person in connection with the sale or attempted sale of such Tax-Exempt Bonds); provided, however, that no Tax-Exempt Lender shall be required to indemnify any indemnified

person for any claims, damages, losses, liabilities, costs or expenses to the extent caused by the willful misconduct or gross negligence of such indemnified person.

The State and the Department acknowledge that a Tax-Exempt Lender may prepare and circulate to potential investors in its tender option program, from time to time, offering circulars with respect to the Tax-Exempt Bonds (or any interest therein) of such Tax-Exempt Lender. Consistent with Section 9.17, unless the State and the Department otherwise consent in writing, no Tax-Exempt Lender shall permit the use of any information in such offering circulars which is not publicly available. Neither the State nor the Department makes any representation as to accuracy or correctness of any information contained in any such offering circular, and each offering circular shall contain a statement to such effect. Neither the State nor the Department have any obligation or duty to review or participate in the preparation of any such offering circular.

9.17. Confidential Treatment. The Agent and the Lenders agree to maintain the confidentiality of all books, accounts and records regarding the State and the Department which are not otherwise publicly available, including, without limitation, power supply agreements; provided, however, that the Agent and the Lenders shall not be precluded from disclosing such information or the contents of such books, accounts, records and agreements (a) to its officers, directors, employees, agents, attorneys and accountants who have a need to know such books, accounts, records or agreements in accordance with customary banking practices and who receive such books, accounts, records or agreements having been made aware of the restrictions set forth in this Section 6.2, (b) to any actual or proposed Participant or Lender which has agreed in writing to be bound by the provisions of this Section 9.17, (c) to the extent disclosure is required by law, statute, rule, regulation or judicial process or (d) upon the lawful demand of any court or agency having jurisdiction over the Agent or any Lender or Participant or pursuant to subpoena.

9.18. Credit Enhancement. With the consent of the Department (which consent shall not be unreasonably withheld), any Lender may seek credit enhancement on all or any portion of its Loan(s) at its own expense. Any Lender which decides to seek credit enhancement will notify the Department and coordinate such Lender's enhancement activities with those of the Department and any other Lender seeking similar enhancement.

9.19. Recharacterization of Loans. If, on or after the Term Out Period Commencement Date, any Lender with a Taxable Loan shall so request in writing to the Department and the Agent (and the Agent shall provide written notice thereof to each other Lender with Taxable Loans), the Department shall, at the expense of such Lender and any other similarly situated Lender that so requests, promptly engage nationally-recognized bond counsel that is reasonably satisfactory to such Lender(s) to determine whether any of the uses for which the proceeds of Taxable Loans were expended by the Department could at the time of issuance, but for the absence of sufficient Tax-Exempt Commitments, Additional Tax-Exempt Commitments and Additional Tax-Exempt Commitments, have supported the issuance of Water Code Bonds the interest on which is excluded from gross income for U.S. federal income tax purposes ("Additional Tax-Exempt Purposes"). In the event that such bond counsel determines that Additional Tax-Exempt Purposes exist, then the Department will use reasonable efforts to substitute Taxable Bonds and the Taxable Loans evidenced thereby with new Water Code Bonds the interest on which is excluded from gross income for U.S. federal income tax purposes. Any such substitution shall be made on a *pro rata* basis among the Taxable Bonds of those Lenders

that are willing to substitute their Taxable Bonds (or portions thereof) for such new Water Code Bonds and that are willing to share the costs of bond counsel on a *pro rata* basis. Any new Water Code Bonds issued pursuant to this Section 9.19 shall, notwithstanding anything to the contrary contained in this Agreement, be considered "Tax-Exempt Bonds" for all purposes of the Transaction Documents and the Debt evidenced thereby shall be considered "Tax-Exempt Loans" for all purposes of the Transaction Documents. Each Lender agrees that "reasonable efforts" would not include a "reissuance" of Bonds.

* * *

IN WITNESS WHEREOF, the parties hereto have caused their duly authorized officers to execute and deliver this Agreement as of the date first above written.

STATE OF CALIFORNIA
Acting by and through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director of Water Resources

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK, as Agent and a Lender

By: William P. Hansen, Jr.
Title: WILLIAM P. HANSEN, JR.
VICE PRESIDENT

JPMORGAN CHASE & CO., as a Lender

By: _____

Title: VP

LEHMAN COMMERCIAL PAPER INC., as a Lender

By: _____

Title: Managing Director

COMMERZBANK AKTIENGESELLSCHAFT,
New York Branch

By: _____
Title: THOMAS J. CARNEY
Senior Vice President

By: _____
Title: Edward C. Neu
Vice President

BAYERISCHE LANDESBANK
GIROZENTRALE, acting through its
New York Branch

By: _____
Title: Scott M. Allison
First Vice President

By: _____
Title: John A. Wain
First Vice President

SCHEDULE 1
TO CREDIT AGREEMENT

COMMITMENTS

Name of Lender	Taxable Commitment	Tax-Exempt Commitment	Total Commitment
Morgan Guaranty Trust Company of New York	$1,500,000,000	$	$1,500,000,000
JPMorgan Chase & Co.		1,000,000,000	1,000,000,000
Lehman Commercial Paper Inc.		1,000,000,000	1,000,000,000
Commerzbank AG	500,000,000		500,000,000
Bayerische Landesbank Girozentrale	300,000,000		300,000,000
Totals:	$2,300,000,000	$2,000,000,000	$4,300,000,000

SCHEDULE 2
TO CREDIT AGREEMENT

NOTICE OFFICE AND LENDING OFFICE

Lender	Notice Office	Lending Office
Morgan Guaranty Trust Company of New York	For Credit Matters: 60 Wall Street New York, NY 10260-0060 Attention: William P. Hansen, Jr. Telephone: 212-648-6819 Facsimile: 212-6485256 For Administrative Matters: c/o J.P. Morgan Services, Inc. 500 Stanton Christiana Road Newark, DE 19713 Attention: Tia R. Truxon Telephone: 302-634-4657 Facsimile: 302-634-1094	c/o J.P. Morgan Services, Inc. 500 Stanton Christiana Road Newark, DE 19713
Lehman Commercial Paper Inc.	For Credit Matters: 3 World Financial Center 9th Floor New York, NY 10285 Attention: Michael Whang Telephone: 212-528-6027 For Administrative Matters: 3 World Financial Center 9th Floor New York, NY 10285 Attention: Michael Whang Telephone: 212-528-6027	3 World Financial Center 9th Floor New York, NY 10285

JPMorgan Chase & Co.	For Credit Matters: 60 Wall Street New York, NY 10260-0060 Attention: William P. Hansen, Jr. Telephone: 212-648-6819 Facsimile: 212-6485256 For Administrative Matters: c/o J.P. Morgan Services, Inc. 500 Stanton Christiana Road Newark, DE 19713 Attention: Tia R. Truxon Telephone: 302-634-4657 Facsimile: 302-634-1094	c/o J.P. Morgan Services, Inc. 500 Stanton Christiana Road Newark, DE 19713 Attention: Lung Ho Telephone: 302-634-1889 Facsimile: 302-634-1852
Commerzbank AG	For Credit Matters: 2 World Financial Center New York, NY 10281 Attention: Edward C. Neu Telephone: 212-266-7508 Facsimile: 212-266-7530 For Administrative Matters: 2 World Financial Center New York, NY 10281 Attention: Christine Scaffidi Telephone: 212-266-7508 Facsimile: 212-266-7530	2 World Financial Center New York, NY 10281
Bayerische Landesbank Girozentrale	For Credit Matters: 560 Lexington Avenue, 18th Floor New York, NY 10022 Attention: James Binette Telephone: 212-310-9863 Facsimile: 212-230-9114 For Administrative Matters: 560 Lexington Avenue, 18th Floor New York, NY 10022 Attention: Patricia Sanchez Telephone: 212-310-9810 Facsimile: 212-310-9930	560 Lexington Avenue, 18th Floor New York, NY 10022

SCHEDULE 3
TO CREDIT AGREEMENT

LITIGATION

1. *In re Pacific Gas and Electric Company,* United States Bankruptcy Court Case No. 01-30923 DM, and related adversarial proceeding against the California Public Utilities Commission

2. California Public Utilities Commission Matters:

A. Challenges to decision of the California Public Utilities Commission:

(1) Decision # 01-04-005 (4/03/01) - Petition for Writ of Review of denials of Applications for Rehearing filed by Pacific Gas & Electric v. California Public Utilities Commission (1st DCA, Case No. A-095132); Southern California Edison v. California Public Utilities Commission (2nd DCA, Case No. B-150523); and CE Generation v. California Public Utilities Commission (4th DCA, Case No. D-038127).

(2). Decision # 01-03-082 (3/27/01) - Applications for Rehearing filed by Pacific Gas & Electric, San Diego Gas & Electric, Leprino Foods, and THE UTILITY REFORM NETWORK (TURN) are pending.

(3) Decision # 01-03-081 (3/27/01) - Applications for Rehearing filed by Pacific Gas & Electric and Southern California Edison are pending.

(4) Decision # 01-03-009 (3/07/01) - An Application for Rehearing filed by Pacific Gas & Electric is pending.

(5) Decision # 01-01-061 (1/31/01) - Petition for Writ of Review of denial of Application for Rehearing filed by San Diego Gas & Electric (4th DCA, Case No. D038064).

(6) Decision # 01-05-037 (5/3/01) - Petition for Writ of Review of denials of Applications for Rehearing filed by Pacific Gas & Electric (1st DCA, Case No. A-095132) and Southern California Edison (2nd DCA, Case No. B-150523), consolidated with Petitions for Writ of Review from Decision # 01-04-005.

B. Various applications, filings, and orders in the following proceedings:

(1) Application of Southern California Edison Company (E 3338-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs. (Application 00-11-038, filed November 16, 2000)

(2) Emergency Application of Pacific Gas and Electric Company to Adopt a Rate Stabilization Plan (U 39 E). (Application 00-11-056, filed November 22, 2000)

(3) Petition of TURN for Modification of Resolution (E-3525). (Application 00-10-028, filed October 17, 2000)

3. *Duke Energy Trading and Marketing v. Davis, et al.* (U.S. District Court, C.D. Cal.), a challenge to the Governor's orders commandeering block forward market contracts.

4. *Tucson Electric v. Davis and California Power Exchange* is a matter pending before Federal Energy Regulatory Commission ("FERC"), a challenge to the Governor's orders commandeering block forward contracts.

5. Claims filed with the State Victim Compensation and Government Claims Board seeking compensation from the State as a result of the commandeering by the Governor under Executive Orders of certain block forward power purchase contracts from Southern California Edison Company and Pacific Gas and Electric Company in February 2001.

6. *Howard Jarvis Taxpayers Association et al.* v. *Kathleen Connell* - No Merit Opinion.

7. *Hendricks v. Hannigan* - No Merit Opinion.

EXECUTIVE DEPARTMENT

STATE OF CALIFORNIA

EXECUTIVE ORDER D-42-01
by the
Governor of the State of California

WHEREAS, on January 17, 2001, I proclaimed a State of Emergency to exist within the State of California due to the existing energy shortage in the State of California and ordered that the Department of Water Resources, separate and apart from its powers and responsibilities with respect to the State Water Resources Development System, shall enter into contracts and arrangements for the purchase and sale of electric power with public and private entities and individuals as may be necessary to assist in mitigating the effects of this emergency (the "Proclamation"); and

WHEREAS, the contracts and agreements authorized by the Proclamation will require financial resources in addition to the significant resources already expended and it is necessary that the Department of Water Resources (the "Department"), on my behalf, be authorized to accept loans that are offered to the State by persons, firms or corporations for the purpose of mitigating the effects of this emergency, as more fully set forth in this Order; and

WHEREAS, the proceeds of loans authorized hereby are needed currently to provide funds for the purchase of power and related costs as provided herein and thereby to mitigate the emergency described in the Proclamation, and therefore at this time it is not possible or practicable to use the proceeds of any such loan to repay to the General Fund any advances heretofore made to the Department from appropriations made to the Department of Water Resources Electric Power Fund (established in Section 80200 and Division 27 of the Water Code as defined below; the "Fund") from the General Fund, or any General Fund moneys expended by the Department pursuant to the Proclamation; and

WHEREAS, it is necessary to effectuate my Proclamation by defining with greater specificity the role of the Department and the Public Utilities Commission (the "Commission") under the Proclamation in preventing widespread and prolonged disruption in electric service in California and the continuing threat of such disruption; and

WHEREAS, the Proclamation and this Executive Order together constitute authority for, and direction to, the Department to accept one or more loans as described herein, and constitute complete, separate and alternative authority for the powers, obligations and activities described in Division 27 of the Water Code, as adopted by Statutes 2001, 1st Extraordinary Session, Chapter 4 and as it shall be amended upon the effective date of Statutes 2001, 1st Extraordinary Session, Chapter 9 ("Division 27"), and the intent of this Order is to authorize and direct the Department to accept loans as described herein and in connection therewith to authorize and confirm as necessary to mitigate the emergency described in the Proclamation the powers, obligations and activities described in Division 27, to the extent not inconsistent with this Order;

NOW, THEREFORE, I, GRAY DAVIS, Governor of the State of California, in accordance with the authority vested in me by the California Emergency Services Act (Chapter 7, Article 3, Division 1, Title 2 of the Government Code, Sections 8550 et. seq.; the "Act"), and in particular, Section 8567 of the Government Code, and in furtherance of my Proclamation of a State of Emergency, hereby issue this order to become effective immediately:

A. Pursuant to Section 8647 of the Act, on my behalf the Department is authorized and directed to accept loans, and to evidence such loans by the issuance of bonds, notes and other obligations of the Department which it deems necessary or appropriate to finance its purchase of electric power or natural gas for the generation of electric power and other costs related thereto (as more specifically authorized by paragraph B of this Order) or to refund such loans, with the prior written approval of the Treasurer and the prior written approval of the Director of Finance. The loans accepted pursuant to this Order may not exceed, in the aggregate (not including loans accepted to refund loans previously accepted hereunder) a principal amount of five billion dollars ($5,000,000,000). Loans accepted pursuant to this Order shall not be deemed to constitute a debt or liability of the State or any political subdivision thereof, other than the Department, or a pledge of the faith and credit of the State or of any such political subdivision, but shall be payable solely from the Fund and as otherwise provided for in the agreement pursuant to which such loans are accepted. Neither the faith and credit nor the taxing power of the State of California shall be pledged to the payment of the principal or interest on the loans so accepted. The acceptance of the loans shall not directly or indirectly obligate the State or any political subdivision thereof to levy or to pledge any form of taxation whatever therefor or to make any appropriation from the General Fund for the payment of loan.

B. The Department is authorized and directed to utilize the proceeds of the loans to make payments on or after the date hereof to purchase electric power and purchase natural gas to be used for the generation of electric power and to pay costs related thereto and to fund capitalized interest and reserves required in connection with such loans.

C. In addition, the Department and the Commission (and their officers and any persons executing any documents in connection with the loans accepted pursuant to this Order) are hereby granted, and directed to exercise, the powers, authorities and rights and granted all the protections described in Division 27 as if set forth herein, including but not limited to, the authority and obligation to provide for the payment (including from the Fund) and security (including, but not limited to, the Department's entitlement to the recovery of its revenue requirements, and such pledges and other covenants as may be necessary or desirable to meet the conditions of the loans and to induce such loans at favorable interest rates) for the loans authorized hereby.

D. The principal amount of any future bonds issued pursuant to Division 27 plus the outstanding principal amount of any loans accepted hereunder and not retired by those future bonds shall not exceed the maximum principal amount of bonds authorized under Statutes 2001, 1st Extraordinary Session, Chapter 9.

I FURTHER DIRECT that as soon as hereafter possible, this order be filed in the Office of the Secretary of State and that widespread publicity and notice be given to this order.

IN WITNESS WHEREOF, I have hereunto set my hand and caused the Great Seal of California to be affixed this 18th day of June 2001.

Gray Davis

Governor of California

ATTEST:

Bill Jones

Secretary of State

EXECUTIVE DEPARTMENT

STATE OF CALIFORNIA

PROCLAMATION
by the
Governor of the State of California

WHEREAS, shortages of electricity available to California's utilities have today resulted in blackouts affecting millions of Californians; and

WHEREAS, unanticipated and dramatic increases in the price of electricity have threatened the solvency of California's major public utilities, preventing them from continuing to acquire and provide electricity sufficient to meet California's energy needs; and

WHEREAS, the California Public Utilities Commission, the Independent Systems Operator and the Electricity Oversight Board have advised that the electricity presently available from California's utilities is insufficient to prevent widespread and prolonged disruption of electric service within California; and

WHEREAS, this energy shortage requires extraordinary measures beyond the authority vested in the California Public Utilities Commission; and

WHEREAS, the imminent threat of widespread and prolonged disruption of electrical power to California's emergency services, law enforcement, schools, hospitals, homes, businesses and agriculture constitutes a condition of extreme peril to the safety of persons and property within the state which, by reason of its magnitude, is likely to be beyond the control of the services, personnel, equipment, and facilities of any single county or city; and

WHEREAS, under the provisions of Section 8558 (b) of the California Government Code, I find that an emergency exists;

NOW, THEREFORE, I, GRAY DAVIS, Governor of the State of California, in accordance with the authority vested in me by the California Emergency Services Act, and in particular, Section 8625 of the California Government Code, **HEREBY PROCLAIM A STATE OF EMERGENCY** to exist within the State of California; and

IT IS ORDERED that all agencies of the state government utilize and employ state personnel, equipment and facilities for the performance of any and all activities to alleviate this emergency.

IT IS FURTHER ORDERED that the Department of Water Resources, separate and apart from its powers and responsibilities with respect to the State Water Resources Development System, shall enter into contracts and arrangements for the purchase and sale of electric power with public and private entities and individuals as may be necessary to assist in mitigating the effects of this emergency. The Department is hereby directed to enter into these contracts as expeditiously as possible and is hereby authorized to do so notwithstanding the provisions of the Government Code and the Public Contract Code applicable to state contracts, including but not limited to, advertising and competitive bidding requirements, which provisions are suspended pursuant to Government Code section 8571 to the extent that they would prevent, hinder or delay the prompt mitigation of the effects of this emergency. The Department is further directed to maintain as separate and distinct the obligations incurred and the funding of such contracts and arrangements from the funds, monies and obligations of the State Water Resources Development System.

I FURTHER DIRECT that as soon as hereafter possible, this proclamation be filed in the Office of the Secretary of State and that widespread publicity and notice be given to this proclamation.

IN WITNESS WHEREOF I have hereunto set my hand and caused the Great Seal of the State of California to be affixed this 17th day of January 2001.

Gray Davis

Governor of California

ATTEST:

Secretary of State

CALIFORNIA DEPARTMENT OF WATER RESOURCES
DETERMINATION TO ISSUE BONDS

The undersigned, as Director (the "Director") of the California Department of Water Resources (the "Department"), hereby determines as follows:

1. This Determination constitutes a written determination to accept loans pursuant loans and issue bonds of the Department pursuant to Division 27 (commencing with Section 80000) of the California Water Code ("Division 27") and the Executive Order D-42-01 of the Governor of the State of California, dated June 18, 2001 (the "Executive Order"), and is executed and delivered pursuant to Section 80132(a) of the California Water Code and the Executive Order.

2. The Department is executing and delivering a Credit and Security Agreement dated June 26, 2001, among the State of California acting through the Department, various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). All terms used and not otherwise defined in this Determination shall have the respective meanings ascribed thereto in the Agreement.

3. Borrowings shall be made by the Department and, to evidence the obligation of the Department to repay such Borrowings, Bonds of the Department secured by the Water Code Collateral are hereby authorized to be issued, in each case under, pursuant to and in accordance with the Agreement, in the aggregate principal amount of $4,300,000,000 (respectively, the "Borrowings" and the "Bonds"). Borrowings in the aggregate principal amount of $2,300,000,000 shall consist of Taxable Loans by the Initial Lenders with a Taxable Commitment, each in the amount of its respective Taxable Commitment, and a Taxable Bond shall be issued to each such Initial Lender in a principal amount equal to the amount of its Taxable Loan. Borrowings in the aggregate principal amount of $2,000,000,000 shall consist of Tax-Exempt Loans by Initial Lenders with a Tax-Exempt Commitment, each in the amount of its respective Tax-Exempt Commitment, and a Tax-Exempt Bond shall be issued to each such Initial Lender in a principal amount equal to the amount of its Tax-Exempt Loan. Such Taxable Loans and Tax-Exempt Loans are hereinafter referred to collectively as the "Loans". The Bonds shall be sold at the prices and in the manner, and on the terms and conditions, and shall contain such other provisions, conditions and limitations (all of which are hereby deemed to be reasonable and proper for the security of the holders of the Bonds) and shall mature at such time or times, and bear interest at such rate or rates, as are specified in the Agreement, which Agreement is herein incorporated by reference as if set forth herein.

4. The proceeds of the Borrowings and, without duplication, the Loans and Bonds, shall be used solely for purposes as authorized by Division 27 and the Executive Order, and all moneys deposited to the Department of Water Resources Electric Power Fund established by Senate Bill 7X and continued by Section 80200 of California Water Code as the Electric Power Fund pursuant to the Act (the "Electric Power Fund") are hereby determined to be necessary to carry out the purposes for which the Electric Power Fund was created, in accordance with Division 27 and the Executive Order.

5. The Department anticipates refunding or retiring the Bonds by issuing long-term indebtedness pursuant to Division 27 on or before October 31, 2001. However, the debt service on the Bonds, to the extent payable from the Electric Power Fund, is not expected to exceed the amounts expected to be available in the Electric Power Fund for their payment.

6. As contemplated by Section 80130 of the California Water Code, a mechanism has been established to ensure that the Loans and the Bonds will be repaid on a timely basis from the Revenues and the other Collateral, consisting, among other things, of the following:

A. AB1X, as amended by SB31X, effective August 15, 2001;

B. Executive Order

C. CPUC Decision No. 01-03-009;

D. CPUC Decision No. 01-03-081;

E. CPUC Decision No. 01-04-005;

F. the Department's acceptance dated June 26, 2001, of D.01-04-005;

G. the Agreement; and

H. this Determination.

7. No Event of Default or Event of Noncompliance has occurred or exists under the Agreement.

8. The Closing Date under the Agreement shall be June 26, 2001, on which date the Borrowings shall be made and such Bonds shall be issued and delivered.

9. The Director is authorized to execute the Agreement and the other Transaction Documents, make the Borrowings and execute the Bonds; the Deputy Director of the Department (the "Deputy Director") is authorized to execute the Bonds and the Agreement, the other Transaction Documents, and the Bonds are authorized to be delivered by any Authorized Representative on behalf of the Department.

10. The Director, the Deputy Director, the Chief of Fiscal Services, the Deputy Controller and all other employees and agents of the Department are authorized to take all actions, and to execute and deliver all certificates, agreements and other instruments, necessary to consummate the transactions contemplated hereby and by the Agreement.

Dated: June 26, 2001.

Thomas M. Hannigan
Director, California Department of Water Resources

CALIFORNIA STATE TREASURER
APPROVAL OF ISSUANCE OF BONDS

The undersigned, as California State Treasurer, hereby:

1. Acknowledges receipt of a Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department of Water Resources (the "Department"), various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). All terms used and not otherwise defined in this Approval shall have the respective meanings ascribed thereto in the Agreement.

2. Acknowledges receipt of the Executive Order, a Determination to Issue Bonds dated the date hereof (the "Determination"), executed by the Director of the Department, authorizing borrowings and the issuance of Bonds under and pursuant to the Agreement in the aggregate principal amount of $4,300,000,000, consisting of $2,300,000,000 aggregate principal amount of Taxable Loans and, without duplication, Taxable Bonds, and $2,000,000,000 aggregate principal amount of Tax-Exempt Loans and, without duplication, Tax-Exempt Bonds.

3. Pursuant to the Executive Order, Section 80132(a) of the California Water Code and Sections 5702 and 5703 of the California Government Code, approves (i) the acceptance of the Loans from such Lenders and the sale of such Bonds under and pursuant to the Determination and the Agreement, (ii) the issuance of such Bonds under and pursuant to the Determination and the Agreement, and (iii) the terms and provisions of such Bonds and of the Agreement.

4. Certifies that the selection of the Lenders was conducted in accordance with Section 5703 of the California Government Code, and as such, this approval constitutes a written finding that the conditions specified in Section 5703(c) are met.

Dated: June 26, 2001.

Philip Angelides
California State Treasurer

CERTIFICATE OF THE DIRECTOR OF FINANCE
OF THE STATE OF CALIFORNIA
AS TO DELIVERY OF DETERMINATION

The undersigned, Director of Finance of the State of California, hereby certify that, on June 25, 2001, I caused delivery of the attached notice of Determination of the Department of Water Resources to Issue Bonds to be made to the persons to whom such notice was addressed, and that such notice was accepted at the offices of such persons on such date.

Dated: June 26, 2001.

B. Timothy Gage
Director of Finance, State of California

Attachment: Notice of Determination

DIRECTOR OF FINANCE
OF THE STATE OF CALIFORNIA
APPROVAL OF ISSUANCE OF BONDS

The undersigned, as Director of Finance of the State of California, hereby:

1. Acknowledges receipt of a Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department of Water Resources (the "Department"), various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). All terms used and not otherwise defined in this Approval will have the respective meanings ascribed thereto in the Agreement.

2. Acknowledges receipt of the Executive Order, a Determination to Issue Bonds dated the date hereof (the "Determination"), executed by the Director of the Department, authorizing borrowings and the issuance of Bonds under and pursuant to the Agreement in the aggregate principal amount of $4,300,000,000 consisting of $2,300,000,000 aggregate principal amount of Taxable Loans and, without duplication, Taxable Bonds, and $2,000,000,000 aggregate principal amount of Tax-Exempt Loans and, without duplication, Tax-Exempt Bonds.

3. Pursuant to the Executive Order, Section 80132(a) of the California Water Code, approves (i) the acceptance of such Loans and the issuance of such Bonds under and pursuant to the Determination and the Agreement, and (ii) the terms and provisions of such Bonds and of the Agreement.

4. Certifies that pursuant to Section 80132(a) of the California Water Code, the undersigned notified the Chairperson of the Joint Legislative Budget Committee, the Chairperson of the committee of the California State Senate that considers appropriations (the Appropriations Committee), the Chairperson of the committee of the California State Assembly that considers appropriations (the Appropriations Committee), and the Chairperson of the Assembly Budget Committee of both the Determination and the approvals of the California State Treasurer and Director of Finance of the State of California required by said Section 80132(a), and delivered to each of such Chairpersons a copy of the Notice of Determination of Department of Water Resource to Issue Bonds in the form attached hereto, all on June 26, 2001.

Dated: June 26, 2001.

B. Timothy Gage
Director of Finance, State of California

Attachment: Notice of Determination of Department of Water Resource to Issue Bonds

NOTICE OF DETERMINATION OF
DEPARTMENT OF WATER RESOURCES
TO ISSUE BONDS

TO: Honorable Steve Peace, Chair, Joint Legislative Budget Committee
Chair, Budget and Fiscal Review Committee
of the California State Senate
Honorable Tony Cardenas, Chair, Budget Committee of the California State Assembly
Honorable Carole Migden, Chair, Appropriations Committee of the
California State Assembly
Honorable Dede Alpert, Chair, Appropriations Committee of the
California State Senate

Pursuant to Executive Order D-42-01 of the Governor of the State of California and Section 80132(a) of the Water Code, this will notify you that the Director of the Department of Water Resources has, on this date, executed a Determination to Issue Bonds in the aggregate principal amount of $4,300,000,000 pursuant to the Executive Order and Division 27 (commencing with Section 80000) of the Water Code, and that the undersigned and the State Treasurer have approved the issuance of such bonds. A copy of such Determination is attached.

Dated: June 26, 2001.

B. Timothy Gage
Director of Finance, State of California

Attachment: Determination to Issue Bonds

CALIFORNIA DEPARTMENT OF WATER RESOURCES
DETERMINATION TO ISSUE BONDS

The undersigned, as Director (the "Director") of the California Department of Water Resources (the "Department"), hereby determines as follows:

1. This Determination constitutes a written determination to accept loans pursuant loans and issue bonds of the Department pursuant to Division 27 (commencing with Section 80000) of the California Water Code ("Division 27") and the Executive Order D-42-01 of the Governor of the State of California, dated June 18, 2001 (the "Executive Order"), and is executed and delivered pursuant to Section 80132(a) of the California Water Code and the Executive Order.

2. The Department is executing and delivering a Credit and Security Agreement dated June 26, 2001, among the State of California acting through the Department, various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). All terms used and not otherwise defined in this Determination shall have the respective meanings ascribed thereto in the Agreement.

3. Borrowings shall be made by the Department and, to evidence the obligation of the Department to repay such Borrowings, Bonds of the Department secured by the Water Code Collateral are hereby authorized to be issued, in each case under, pursuant to and in accordance with the Agreement, in the aggregate principal amount of $4,300,000,000 (respectively, the "Borrowings" and the "Bonds"). Borrowings in the aggregate principal amount of $2,300,000,000 shall consist of Taxable Loans by the Initial Lenders with a Taxable Commitment, each in the amount of its respective Taxable Commitment, and a Taxable Bond shall be issued to each such Initial Lender in a principal amount equal to the amount of its Taxable Loan. Borrowings in the aggregate principal amount of $2,000,000,000 shall consist of Tax-Exempt Loans by Initial Lenders with a Tax-Exempt Commitment, each in the amount of its respective Tax-Exempt Commitment, and a Tax-Exempt Bond shall be issued to each such Initial Lender in a principal amount equal to the amount of its Tax-Exempt Loan. Such Taxable Loans and Tax-Exempt Loans are hereinafter referred to collectively as the "Loans". The Bonds shall be sold at the prices and in the manner, and on the terms and conditions, and shall contain such other provisions, conditions and limitations (all of which are hereby deemed to be reasonable and proper for the security of the holders of the Bonds) and shall mature at such time or times, and bear interest at such rate or rates, as are specified in the Agreement, which Agreement is herein incorporated by reference as if set forth herein.

4. The proceeds of the Borrowings and, without duplication, the Loans and Bonds, shall be used solely for purposes as authorized by Division 27 and the Executive Order, and all moneys deposited to the Department of Water Resources Electric Power Fund established by Senate Bill 7X and continued by Section 80200 of California Water Code as the Electric Power Fund pursuant to the Act (the "Electric Power Fund") are hereby determined to be necessary to carry out the purposes for which the Electric Power Fund was created, in accordance with Division 27 and the Executive Order.

5. The Department anticipates refunding or retiring the Bonds by issuing long-term indebtedness pursuant to Division 27 on or before October 31, 2001. However, the debt service on the Bonds, to the extent payable from the Electric Power Fund, is not expected to exceed the amounts expected to be available in the Electric Power Fund for their payment.

6. As contemplated by Section 80130 of the California Water Code, a mechanism has been established to ensure that the Loans and the Bonds will be repaid on a timely basis from the Revenues and the other Collateral, consisting, among other things, of the following:

A. AB1X, as amended by SB31X, effective August 15, 2001;

B. Executive Order

C. CPUC Decision No. 01-03-009;

D. CPUC Decision No. 01-03-081;

E. CPUC Decision No. 01-04-005;

F. the Department's acceptance dated June 26, 2001, of D.01-04-005;

G. the Agreement; and

H. this Determination.

7. No Event of Default or Event of Noncompliance has occurred or exists under the Agreement.

8. The Closing Date under the Agreement shall be June 26, 2001, on which date the Borrowings shall be made and such Bonds shall be issued and delivered.

9. The Director is authorized to execute the Agreement and the other Transaction Documents, make the Borrowings and execute the Bonds; the Deputy Director of the Department (the "Deputy Director") is authorized to execute the Bonds and the Agreement, the other Transaction Documents, and the Bonds are authorized to be delivered by any Authorized Representative on behalf of the Department.

10. The Director, the Deputy Director, the Chief of Fiscal Services, the Deputy Controller and all other employees and agents of the Department are authorized to take all actions, and to execute and deliver all certificates, agreements and other instruments, necessary to consummate the transactions contemplated hereby and by the Agreement.

Dated: June 26, 2001.

Thomas M. Hannigan
Director, California Department of Water Resources

State of California

SECRETARY OF STATE

I, *BILL JONES*, Secretary of State of the State of California, hereby certify:

That the attached transcript of 13 page(s) was prepared by and in this office from the record on file, of which it purports to be a copy, and that it is full, true and correct.

IN WITNESS WHEREOF, I execute this certificate and affix the Great Seal of the State of California this

21st day of June 2001

Bill Jones

Secretary of State

(v) Ch 4

FILED
In the office of the Secretary of State
of the State of California

FEB 0 1 2001

At 3:55 O'clock P M.
BILL JONES, Secretary of State
By Marcia Murphey
Deputy Secretary of State

Approved Feb 1, 2001

Gray Davis
Governor

Assembly Bill No. 1

Passed the Assembly FEB 1 2001

E P Olson Wilson
Chief Clerk of the Assembly

Passed the Senate JAN 3 1 2001

Gregg P. Schmidt
Secretary of the Senate

This bill was received by the Governor this 1st day of February, 2001, at 2:15 o'clock P.M.

Pamela K. Oto
Private Secretary of the Governor

CHAPTER 4

An act to amend Section 366.5 of, and to add Section 360.5 to, and to repeal Section 355.1 of, the Public Utilities Code, and to add Division 27 (commencing with Section 80000) to the Water Code, relating to electric power, making an appropriation therefor, and declaring the urgency thereof, to take effect immediately.

LEGISLATIVE COUNSEL'S DIGEST

AB 1, Keeley. Power exchanges: Department of Water Resources: electric power.

(1) The Public Utilities Act establishes the Power Exchange to provide an efficient competitive auction, open on a nondiscriminatory basis to all electric power suppliers, that meets the loads of all exchange customers at efficient prices. Existing law authorizes the Public Utilities Commission to investigate issues associated with multiple qualified exchanges, and requires the commission, if it determines that allowing electrical corporations to purchase from multiple qualified exchanges is in the public interest, to prepare and submit findings and recommendations to the Legislature on or before June 1, 2001. Existing law prohibits the implementation by the commission of certain commission decisions regarding other exchanges, as specified.

This bill would repeal those provisions, regarding multiple qualified exchanges.

(2) Existing law prohibits any change in the aggregator or supplier of electric power for certain customers from being made until the change has been verified.

This bill would provide that electric power sold to customers pursuant to the bill is not subject to those provisions.

(3) Under existing law relating to the Central Valley Project, the Department of Water Resources has the authority to fix and establish the prices, rates, and charges at which the resources and facilities made available by the project are sold and disposed of, and to enter into contracts and agreements and do any and all things that the department determines to be necessary, convenient, or expedient for the accomplishment of the purposes and objectives of that existing law.

This bill would authorize the department to enter into contracts for the purchase of electric power. The bill would authorize the department to sell power to retail end use customers and, with specified exceptions, to local publicly owned electric utilities at not more than the department's acquisition costs, as specified. The bill would prohibit the department from contracting for the purchase of electric power on and after January 2, 2003. The bill would provide, with specified exceptions, that nothing in the bill authorizes the department to take ownership of transmission, generation, or distribution assets, as specified. The bill would also authorize the department to hire and appoint additional employees and contract for the services of public and private entities.

The bill would authorize the department to issue revenue bonds not to exceed a certain amount, containing specified terms and conditions, upon authorization by written determination of the department and with the approval of the Director of Finance and the Treasurer, as specified.

The bill would establish in the State Treasury the Department of Water Resources Electric Power Fund, to be continuously appropriated to the department, and available for the purposes described above. The bill would require all revenues payable to the department under the bill to be deposited in the fund. The bill would require that payments from the fund be made only for certain purposes. The bill would transfer $495,755,000 from the General Fund to the fund for the purposes described above and require repayment to the General Fund at the earliest possible time. The bill would appropriate $4,245,000 to the department for the 2000–01 fiscal year for administrative cost incurred by the department for purposes of the bill. The bill would permit the Department of Finance to authorize the creation of deficiencies for this appropriation.

This bill would require the Public Utilities Commission to calculate the California Procurement Adjustment and would further require the commission to determine the amount of the adjustment payable to the department for deposit into the fund.

The bill would require the Bureau of State Audits to conduct a financial and performance audit of the department's implementation of the bill.

(4) This bill would declare that it is to take effect immediately as an urgency statute.

Appropriation: yes.

The people of the State of California do enact as follows:

SECTION 1. Section 355.1 of the Public Utilities Code is repealed.

SEC. 2. Section 360.5 is added to the Public Utilities Code, to read:

360.5. The commission shall determine that portion of each existing electrical corporation's retail rate effective on January 5, 2001, that is equal to the difference between the generation related component of the retail rate and the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services. That portion of the retail rate shall be known as the California Procurement Adjustment. The commission shall further determine the amount of the California Procurement Adjustment that is allocable to the power sold by the department. That amount shall be payable, by each electrical corporation, upon receipt by the electrical corporation of the revenues from its retail end use customers, to the department for deposit in the Department of Water Resources Electric Power Fund, established by Section 80200 of the Water Code. The amount determined pursuant to this subdivision shall be known as the Fixed Department of Water Resources Set-Aside.

SEC. 3. Section 366.5 of the Public Utilities Code is amended to read:

366.5. (a) No change in the aggregator or supplier of electric power for any small commercial customer may be made until one of the following means of confirming the change has been completed:

(1) Independent third-party telephone verification.

(2) Receipt of a written confirmation received in the mail from the consumer after the consumer has received an information package confirming the agreement.

(3) The customer signs a document fully explaining the nature and effect of the change in service.

(4) The customer's consent is obtained through electronic means, including, but not limited to, computer transactions.

(b) No change in the aggregator or provider of electric power for any residential customer may be made over the telephone until

the change has been confirmed by an independent third-party verification company, as follows:

(1) The third-party verification company shall meet each of the following criteria:

(A) Be independent from the entity that seeks to provide the new service.

(B) Not be directly or indirectly managed, controlled, or directed, or owned wholly or in part, by an entity that seeks to provide the new service or by any corporation, firm, or person who directly or indirectly manages, controls, or directs, or owns more than 5 percent of the entity.

(C) Operate from facilities physically separate from those of the entity that seeks to provide the new service.

(D) Not derive commission or compensation based upon the number of sales confirmed.

(2) The entity seeking to verify the sale shall do so by connecting the resident by telephone to the third-party verification company or by arranging for the third-party verification company to call the customer to confirm the sale.

(3) The third-party verification company shall obtain the customer's oral confirmation regarding the change, and shall record that confirmation by obtaining appropriate verification data. The record shall be available to the customer upon request. Information obtained from the customer through confirmation shall not be used for marketing purposes. Any unauthorized release of this information is grounds for a civil suit by the aggrieved resident against the entity or its employees who are responsible for the violation.

(4) Notwithstanding paragraphs (1), (2), and (3), an aggregator or provider of electric power shall not be required to comply with these provisions when the customer directly calls an aggregator or provider of electric power to change service providers. However, an aggregator or provider of electric power shall not avoid the verification requirements by asking a customer to contact an aggregator or provider of electric power directly to make any change in the service provider.

(c) No change in the aggregator or provider of electric power for any residential customer may be made via an Internet transaction, in which the customer accesses the website of the

aggregator or provider, unless both of the following occur with respect to confirming the change:

(1) In addition to any other information gathered in the course of the transaction, the customer shall be asked to read and respond to a separate screen that states, in easily legible text, the following:

"I acknowledge that in entering this transaction I am voluntarily choosing to change the entity that supplies me with my electric power."

(2) The separate screen shall offer the customer the option to complete or terminate the transaction.

(d) (1) No change in the aggregator or provider of electric power for any residential customer may be made via a written transaction unless the change has been confirmed, as provided in this subdivision. In order to comply with this subdivision, in addition to any other information gathered in the course of the transaction, and in addition to any other signature required, the customer shall be asked to sign and date a document separate from that written transaction, containing the following words printed in 10-point type or larger:

"I acknowledge that in signing this contract or agreement, I am voluntarily choosing to change the entity that supplies me with electric power."

(2) The acknowledgment document described in paragraph (1) may not be included with a check or in connection with a sweepstakes solicitation.

(e) Any aggregator or provider of electric power offering electricity service to residential and small commercial customers that switches the electric service of a customer without the customer's consent shall be liable to the aggregator or provider of electric power offering electricity services previously selected by the customer in an amount equal to all charges paid by the customer after the violation and shall refund to the customer any amount in excess of the amount that the customer would have been obligated to pay had the customer not been switched.

(f) An aggregator or provider of electric power shall keep a record of the confirmation of a change pursuant to subdivision (b), (c), or (d) for two years from the date of that confirmation, and shall make those records available, upon request, to the customer and to the commission in the course of a commission investigation

of a customer complaint or an investigation pursuant to subdivision (c) of Section 394.2.

(g) Public agencies are exempt from this section to the extent they are serving customers within their jurisdiction.

(h) Notwithstanding subdivisions (c) and (d), the commission may require third-party verification for all residential changes to electric service providers if it finds that the application of subdivisions (c) and (d) results in the unauthorized changing of a customer's electric service provider.

(i) An electrical corporation is exempt from this section for customers that default to the service of the electrical corporation.

(j) Electric power sold to customers pursuant to Section 80100 of the Water Code is not subject to this section.

SEC. 4. Division 27 (commencing with Section 80000) is added to the Water Code, to read:

DIVISION 27. PURCHASE AND SALE OF ELECTRIC POWER

CHAPTER 1. GENERAL PROVISIONS AND DEFINITIONS

80000. The Legislature hereby finds and declares all of the following:

(a) The furnishing of reliable reasonably priced electric service is essential for the safety, health, and well-being of the people of California. A number of factors have resulted in a rapid, unforeseen shortage of electric power and energy available in the state and rapid and substantial increases in wholesale energy costs and retail energy rates, with statewide impact, to such a degree that it constitutes an immediate peril to the health, safety, life and property of the inhabitants of the state, and the public interest, welfare, convenience and necessity require the state to participate in markets for the purchase and sale of power and energy.

(b) In order for the department to adequately and expeditiously undertake and administer the critical responsibilities established in this division, it must be able to obtain, in a timely manner, additional and sufficient personnel with the requisite expertise and experience in energy marketing, energy scheduling, and accounting.

80002. Nothing in this division shall be construed to reduce or modify any electrical corporation's obligation to serve. The commission shall issue orders it determines are necessary to carry out this section. Nothing in this section shall be construed to obligate the department for any procurement cost obligations of any electrical corporation that may have existed as of the effective date of this section.

80002.5. It is the intent of the Legislature that power acquired by the department under this division shall be sold to all retail end use customers being served by electrical corporations, and may be sold, to the extent practicable, as determined by the department, to those local publicly owned electric utilities requesting such power. Power sold by the department to retail end use customers shall be allocated pro rata among all classes of customers to the extent practicable.

80003. (a) The development and operation of a program as provided in this division is in all respects for the welfare and the benefit of the people of the state, to protect the public peace, health, and safety, and constitutes an essential governmental purpose.

(b) This division shall be construed in a manner so as to effectuate the purposes and objectives thereof.

80004. (a) The powers and responsibilities of the department established under this division are within the scope of the primary duties of the department, but are not governed by the provisions relating to the State Water Resources Development System.

(b) The Department of Water Resources Electric Purchases Fund, established by Section 80200, and the money in that fund are separate and distinct from any other fund and money administered by the department.

80010. As used in this division, unless the context otherwise requires, the following terms have the following meanings:

(a) "Bonds" means bonds, notes, or other evidences of indebtedness issued solely for the purposes of paying the cost of electric power and transmission, scheduling, and other related expenses incurred by the department on and after the effective date of this division, or to reimburse expenditures from the fund for those purposes; repaying to the General Fund any advances made to the department from appropriations made to the fund pursuant hereto or hereafter for purposes of this division, any advances made to the department from the Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001; establishing or maintaining reserves in connection with the bonds; costs of issuance of bonds or incidental to their payment or security; capitalized interest; or to renew or refund any bonds.

(b) "Commission" means the Public Utilities Commission.

(c) "Electrical corporation" has the same meaning as that term is defined in Section 218 of the Public Utilities Code.

(d) "Fund" means the Department of Water Resources Electric Power Fund established by Section 80200.

(e) "Local publicly owned electric utility" includes the entities defined in subdivision (d) of Section 9604 of the Public Utilities Code and publicly owned utilities that provide electricity.

(f) "Power" means electric power and energy, including, but not limited to, capacity and output, or any of them.

(g) "Public utility" has the same meaning as that term is defined in Section 216 of the Public Utilities Code.

80012. The department shall do those things necessary and authorized under Chapter 2 (commencing with Section 80100) to make power available directly or indirectly to elec consumers

in California. Except as otherwise stated, nothing in this division authorizes the department to take ownership of the transmission, generation, or distribution assets of any electrical corporation in this state.

80014. (a) The department and commission may adopt regulations for purposes of this division as emergency regulations in accordance with Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code. For purposes of that Chapter 3.5, including Section 11349.6 of the Government Code, the adoption of the regulations shall be considered by the Office of Administrative Law to be necessary for the immediate preservations of the public peace, health and safety, and general welfare. Notwithstanding subdivision (e) of Section 11346.1 of the Government Code, the regulations shall be repealed 180 days after their effective date, unless the adopting authority or agency complies with that Chapter 3.5, as provided in subdivision (e) of Section 11346.1 of the Government Code.

(b) Unless the department determines that application of any such provision to such contracts is detrimental to accomplishing the purposes of this division, the provisions of the Government Code and Public Contract Code applicable to state contracts, including, but not limited to, advertising and competitive bidding requirements and prompt payment requirements, apply to contracts entered into under this division.

80016. All state agencies and other official state organizations, and all persons connected therewith, shall and are hereby authorized to, at the request of the department, give the department reasonable assistance or other cooperation in carrying out the purposes of this division.

CHAPTER 2. POWER PROGRAM

Article 1. Powers of the Department

80100. Upon those terms, limitations, and conditions as it prescribes, the department may contract with any person, local publicly owned electric utility, or other entity for the purchase of power on such terms and for such periods as the department determines and at such prices the department deems appropriate taking into account all of the following:

(a) The intent of the program described in this division is to achieve an overall portfolio of contracts for energy resulting in reliable service at the lowest possible price per kilowatthour.

(b) The need to have contract supplies to fit each aspect of the overall energy load profile.

(c) The desire to secure as much low-cost power as possible under contract.

(d) The duration and timing of contracts made available from sellers.

(e) The length of time sellers of electricity offer to sell such electricity.

(f) The desire to secure as much firm and nonfirm renewable energy as possible. Prior to commencement of the program described in this division, the department shall assess the need for power in the state in consultation with the Public Utilities Commission and local publicly owned electric utilities and electrical corporations in the state and such other entities in the state as the department determines are appropriate. The department may also enter into options or forward contracts with respect to the foregoing, and contract with any person, local publicly owned electric utility, or other entity for transmission, scheduling, and other related power services necessary or desirable to accomplish the purposes of this division.

80102. (a) Contracts under this division may provide for the assignment thereof on any terms and conditions as the contracts may specify.

(b) Any contract for the purchase or sale of electric power shall contain any contractual terms and security provisions as are determined by the department to be necessary or appropriate and the department may enter into such arrangements as may be necessary or appropriate to implement the foregoing.

(c) Notwithstanding any other provision of law, the department may pay or provide for the payment of pow r use of

transmission or distribution facilities and other related services prior to the delivery or utilization thereof, provided that the department determines that prepayment is beneficial to ratepayers and that adequate provision has been made for the security of the department.

80104. Upon the delivery of power to them, the retail end use customers shall be deemed to have purchased that power from the department. Payment for any sale shall be a direct obligation of the retail end use customer to the department.

80106. (a) The department may contract with the related electrical corporation or its successor in the performance of related service, for the electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute the power and provide billing, collection, and other related services, as agent of the department, on terms and conditions that reasonably compensate the electrical corporation for its services.

(b) At the request of the department, the commission shall order the related electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute the power and provide billing, collection, and other related services, as agent of the department, on terms and conditions that reasonably compensate the electrical corporation for its services.

80108. The commission may issue rules regulating the enforcement of the agency function pursuant this division, including collection and payment to the department.

80110. The department shall retain title to all power sold by it to the retail end use customers. The department shall be entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to comply with Section 80134, and shall advise the commission as the department determines to be appropriate. Such revenue requirements may also include any advances made to the department hereunder or hereafter for purposes of this division, or from the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001. For purposes of this division and except as otherwise provided in this section, the Public Utility Commission's authority as set forth in Section 451

of the Public Utilities Code shall apply, except any just and reasonable review under Section 451 shall be conducted and determined by the department. The commission may enter into an agreement with the department with respect to charges under Section 451 for purposes of this division, and that agreement shall have the force and effect of a financing order adopted in accordance with Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the Public Utilities Code, as determined by the commission. In no case shall the commission increase the electricity charges in effect on the date that the act that adds this section becomes effective for residential customers for existing baseline quantities or usage by those customers of up to 130 percent of existing baseline quantities, until such time as the department has recovered the costs of power it has procured for the electrical corporation's retail end use customers as provided in this division. After the passage of such period of time after the effective date of this section as shall be determined by the commission, the right of retail end use customers pursuant to Article 6 (commencing with Section 360) of Chapter 2.3 of Part 1 of Division 1 of the Public Utilities Code to acquire service from other providers shall be suspended until the department no longer supplies power hereunder. The department shall have the same rights with respect to the payment by retail end use customers for power sold by the department as do providers of power to such customers.

80112. All money collected with respect to any power acquired and sold pursuant to this division and the Governor's Emergency Proclamation dated January 17, 2001, and all money paid directly or indirectly to or for the account of the department with respect to any sale, exchange, transfer, or disposition of power acquired pursuant hereto, shall constitute property of the department and shall be deposited in the fund in accordance with subdivision (b) of Section 80200. To the extent any moneys are received by an electrical corporation pursuant to Section 80106 in the process of collection, and pending their transfer to the department, they shall be segregated by the electrical corporation on terms and conditions established by the department and shall be held in trust for the benefit of the department.

80114. The commission shall take those actions necessary to ensure that all, or a portion of, the component s that are

available to electrical corporations for the purchase of their net short position of electricity are used to recover the revenue requirements established pursuant to this division.

80116. The department may sell any power acquired by the department pursuant to this division to retail end use customers, and to local publicly owned electric utilities, at not more than the department's acquisition costs, including transmission, scheduling, and other related costs, plus other costs as provided in Section 80200, or exchange power with any person or public or private entity. The department may not sell power to any local publicly owned electric utility, as defined in Section 9604 of the Public Utilities Code, which is itself a net seller of power. However, to the extent that any acquired power is not required for use within the state, if it is otherwise advantageous and necessary, the power may be sold, transferred, or otherwise disposed of, or an option may be granted with respect to the power, to any person or public or private entity. Except to maintain system integrity, the department shall sell the power that is to be delivered to retail end use customers within the service area of the electrical corporations that purchase power from the electrical corporations directly to the retail end use customers.

80120. The department may fix and establish the procedure and charges for the sale or other disposal of power purchased by the department.

80122. The department may do any of the following as may be, in the determination of the department, necessary for the purposes of this division:

(a) Hire and appoint employees as required, at salary levels determined by the director to be competitive to attract and retain persons with the necessary expertise and skills. Prior to hiring or appointing an employee at a salary in excess of a salary approved by the Department of Personnel Administration, the director shall submit the proposed salary to the Director of Finance who shall submit it to the Legislature in accordance with Section 27.00 of the annual Budget Act. No excess salary authorized under this section may be paid on or after January 1, 2003. The excess portion of a salary authorized under this section may not be considered salary in the calculation of final compensation for purposes of benefits under the Public Employees' Retirement System.

(b) Engage the services of private parties to render professional and technical assistance and advice and other services in carrying out the purposes of this division.

(c) Contract for the services of other public agencies.

(d) The State Personnel Board and the Department of Personnel Administration shall assist the department in expediting the hiring of personnel necessary and desirable for the timely and successful implementation and administration of the department's duties and responsibilities pursuant to this division.

CHAPTER 2.5. BONDS

80130. The department may incur indebtedness and issue nds as evidence thereof, provided that bonds may not be issued an amount the debt service on which, to the extent payable from e fund, is expected by the department to exceed the amounts pected to be available in the fund for their payment. In no event all the department authorize the issuance of bonds (excluding tes issued in anticipation of the issuance of bonds and retired n the proceeds of those bonds) in an aggregate amount greater an the amount calculated by multiplying by a factor of four the ual revenues generated by the California Procurement djustment, as determined by the commission pursuant to Section 0.5. In addition, before the issuance of bonds, the department all establish a mechanism to ensure that the bonds will be sold investment grade ratings and repaid on a timely basis from dged revenues. This mechanism may include, but is not limited , an agreement between the department and the commission as scribed in Section 80110.

80132. (a) Bonds may be issued by the department upon thorization by written determination of the director of the partment with the approval of the Director of Finance and the ate Treasurer. The Department of Finance shall notify the airperson of the Joint Legislative Budget Committee and the airperson of the committee in each house that considers propriations of its written determination. The bonds shall be ld at such prices and in such manner, and on such terms and nditions, as shall be specified in such determination, and such termination may contain or authorize any other provision, ndition, or limitation not inconsistent herewith and such ovisions as may be deemed reasonable and proper for the curity of the bondholders. Bonds may mature at such time or nes, and bear interest at such rate or rates, which may be fixed variable and be determined by reference to an index or such her method, as shall be specified in such determination. Neither e person executing the determination to issue bonds nor any rson executing bonds shall be personally liable therefor or be bject to any personal liability or accountability by reason of the suance thereof.

(b) In the discretion of the department, any bonds may be cured by a tru reement by and between the department and

a corporate trustee, which may be any trust company or bank having trust powers within or without the state, or the State Treasurer. Notwithstanding any other provision of law, the State Treasurer shall not be deemed to have a conflict of interest by reason of acting as such trustee. The department may enter into such contracts or arrangements as it shall deem to be necessary or appropriate for the issuance and further security of the bonds.

(c) Bonds shall be legal investments for all trust funds, the funds of all insurance companies, banks both commercial and savings, trust companies, executors, administrators, trustees, and other fiduciaries, for state school funds, pension funds, and, for any funds that may be invested in county, school, or municipal bonds.

(d) Notwithstanding that bonds may be payable from a special fund, they shall be deemed to be negotiable instruments for all purposes.

(e) Any and all bonds, their transfer and the income therefrom shall at all times be free from taxation of every kind by the state and by all political subdivisions of the state.

(f) Bonds shall not be deemed to constitute a debt or liability of the state or of any political subdivision thereof, other than the department, or a pledge of the faith and credit of the state or of any such political subdivision, other than the department, but shall be payable solely from the funds herein provided for. All bonds shall contain a statement to the following effect: "Neither the faith and credit nor the taxing power of the State of California is pledged to the payment of the principal of or interest on this bond." The issuance of bonds shall not directly or indirectly or contingently obligate the state or any political subdivision thereof to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment.

(g) The department may pledge or assign any revenues under any obligation entered into, and rights to receive the same, and moneys on deposit in the fund and income or revenue derived from the investment thereof, as security for the department's obligations hereunder. It is the intention of the Legislature that any pledge of moneys, revenues, or property made by the department shall be valid and binding from the time when the pledge is made; that the moneys, revenues, or property so pledged and thereafter collected from retail end use customers, or paid directly or in tly to or

or the account of the department, is hereby made, and shall immediately be, subject to the lien of such pledge without any physical delivery thereof or further act; that the lien of any such pledge shall be valid and binding as against all parties having claims of any kind in tort, contract, or otherwise against the department irrespective of whether such parties have notice thereof, and that no resolution or instrument by which such pledge or lien created pursuant to this subdivision is expressed, confirmed, or approved need be filed or recorded in order to perfect such pledge or lien. The provisions hereof shall in all respects govern the creation, perfection, priority, and enforcement of any lien created hereby or hereunder.

80134. (a) The department shall, and in any obligation entered into pursuant to this division may covenant to, at least annually, and more frequently as required, establish and revise revenue requirements sufficient, together with any moneys on deposit in the fund, to provide all of the following:

(1) The amounts necessary to pay the principal of and premium, if any, and interest on all bonds as and when the same shall become due.

(2) The amounts necessary to pay for power purchased by it and to deliver it to purchasers, including the cost of electric power and transmission, scheduling, and other related expenses incurred by the department, or to make payments under any other contracts, agreements, or obligations entered into by it pursuant hereto, in the amounts and at the times the same shall become due.

(3) Reserves in such amount as may be determined by the department from time to time to be necessary or desirable.

(4) The pooled money investment rate on funds advanced for electric power purchases prior to the receipt of payment for those purchases by the purchasing entity.

(5) Repayment to the General Fund of appropriations made to the fund pursuant hereto or hereafter for purposes of this division, appropriations made to the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001.

(6) The administrative costs of the department incurred in administering this division.

(b) The department shall notify the commission of its revenue requirement pursuant to Section 80110.

CHAPTER 3. DEPARTMENT OF WATER RESOURCES ELECTRIC POWER FUND

80200. (a) There is hereby established in the State Treasury he Department of Water Resources Electric Power Fund. Notwithstanding Section 13340 of the Government Code, all noneys in the fund are continuously appropriated, without regard o fiscal year, to the department, and shall be available for the purposes of this division. It is the intent of the Legislature that this und be a continuation of the fund created in Chapter 3 of the Statutes of 2001 (SB 7 of the First 2001–02 Extraordinary Session).

(b) All revenues payable to the department under this division hall be deposited in the fund. Notwithstanding any other provision of law, interest accruing on money in the fund shall emain in the fund and shall be used for the purposes of this livision. Payments from the fund may be made only for the purposes authorized by this division, including, but not limited to, payments for any of the following:

(1) The cost of electric power and transmission, scheduling, nd other related expenses incurred by the department.

(2) The pooled money investment rate on funds advanced for electric power purchases prior to the receipt of payment for those purchases by the purchasing entity.

(3) Payment of any bonds or other contractual obligations uthorized by this division.

(4) Repayment to the General Fund of appropriations made to he fund pursuant hereto or hereafter for purposes of this division, ppropriations made to the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the lepartment pursuant to the Governor's Emergency Proclamation lated January 17, 2001. It is the intent of the Legislature that such epayment be made as soon as practicable.

(c) Except as provided in subdivision (b) of Section 5 of the tatute adding this section, the administrative costs of the lepartment incurred in administering this division shall be provided in the annual Budget Act.

(d) Obligations authorized by this division shall be payable olely from the fund. Neither the full faith and credit nor the taxing power of the state are or may be pledged for any payment under ny obligation authorized by this division.

(e) While any obligations of the department incurred under this division remain outstanding and not fully performed or discharged, the rights, powers, duties, and existence of the department and the commission shall not be diminished or impaired in any manner that will affect adversely the interests and rights of the holders of or parties to such obligations. The department may include this pledge and undertaking of the state in the department's obligations.

CHAPTER 4. REPORTING

80250. The department shall make quarterly and annual reports to the Governor and the Legislature regarding its activities and expenditures pursuant to this division.

CHAPTER 5. TERMINATION OF AUTHORITY TO CONTRACT

80260. On and after January 1, 2003, the department shall not contract under this division for the purchase of electrical power. This section does not affect the authority of the department to administer contracts entered into prior to that date or the department's authority to sell electricity.

CHAPTER 6. AUDIT

80270. The Bureau of State Audits shall conduct a financial and performance audit of the department's implementation of this division. The audit shall be completed before December 31, 2001. The bureau shall issue a final report on or before March 31, 2003.

SEC. 5. The following sums are hereby transferred or appropriated from the General Fund, as follows:

(a) Four hundred ninety-five million seven hundred fifty-five thousand dollars ($495,755,000) is hereby transferred to the Department of Water Resources Electric Power Fund, established by Section 80200 of the Water Code, for the purposes of Division 27 (commencing with Section 80000) of the Water Code. The four hundred ninety-five million seven hundred fifty-five thousand dollars ($495,755,000) shall be repaid from the fund to the General Fund at the earliest possible time.

(b) Four million two hundred forty-five thousand dollars ($4,245,000) is appropriated to the department for the 2000–01 fiscal year for the administrative costs incurred by the department for the purposes of Division 27 (commencing with Section 80000) of the Water Code.

SEC. 6. The Department of Finance may authorize the creation of deficiencies for the appropriation made by Section 5 of the act adding this section. No deficiency may be approved under this section any sooner than 10 days after written notification of the proposed deficiency is given to the Chairperson of the Joint Legislative Budget Committee and the chairperson of the committee in each house that considers appropriations.

SEC. 7. This act is an urgency statute necessary for the immediate preservation of the public peace, health, or safety within the meaning of Article IV of the Constitution and shall go into immediate effect. The facts constituting the necessity are:

In order to address the rapid, unforeseen shortage of electric power and energy available in the state and rapid and substantial increases in wholesale energy costs and retail energy rates, that endanger the health, welfare, and safety of the people of this state, it is necessary for this act to take effect immediately.

State of California

SECRETARY OF STATE

I, *BILL JONES*, Secretary of State of the State of California, hereby certify:

That the attached transcript of 6 page(s) was prepared by and in this office from the record on file, of which it purports to be a copy, and that it is full, true and correct.

IN WITNESS WHEREOF, I execute this certificate and affix the Great Seal of the State of California this

21st day of June 2001

Bill Jones

Secretary of State

Sec/State Form CE-108 (rev. 4/97)

FILED
In the office of the Secretary of State
of the State of California

MAY 10 2001

At 2:15 o'clock P M.
BILL JONES, Secretary of State
By Deputy Secretary of State

Approved May 10, 2001

Gray Davis
Governor

Senate Bill No. 31

Passed the Senate May 9, 2001

Secretary of the Senate

Passed the Assembly May 7, 2001

Chief Clerk of the Assembly

This bill was received by the Governor this 9th day of May, 2001, at 11:45 o'clock A.M.

Private Secretary of the Governor

CHAPTER 9

An act to amend Section 1731 of, and to add Section 1768 to, the Public Utilities Code, and to amend Sections 80106, 80130, 80132, and 80200 of, and to repeal Section 80114 of, the Water Code, and to amend and repeal Section 6 of Chapter 4 of the Statutes of 2001 of the First Extraordinary Session, relating to energy, and making an appropriation therefor.

LEGISLATIVE COUNSEL'S DIGEST

SB 31, Burton. Electric power.

(1) Under existing law, after any order or decision has been made by the Public Utilities Commission, any party to the action or proceeding, or any stockholder or bondholder or other party pecuniarily interested in the public utility affected, may apply for a rehearing in respect to any matters determined in the action or proceeding and specified in the application for rehearing.

This bill would prohibit a cause of action arising out of any order or decision of the commission construing, applying, or implementing the provisions of Chapter 4 of the Statutes of 2001–02 First Extraordinary Session (AB 1) from accruing in any court to any corporation or person unless the corporation or person has filed an application to the commission for a rehearing within 10 days after the date of issuance, and the commission would be required to issue its decision and order on rehearing within 20 days after the filing of that application.

This bill would also set forth a specific procedure with regard to judicial review of an order or decision of the commission interpreting, implementing, or applying the provisions of the above referenced Chapter 4.

(2) Existing law authorizes the Department of Water Resources to contract with an electrical corporation to transmit or provide for the transmission of, and distribute the power and provide billing, collection, and other related services, as the agent of the department, on terms and conditions that reasonably compensate the electrical corporation for its services, and requires the commission, at the request of the department, to order such actions. Under existing law, upon the delivery of power to them,

the retail end-use customers are deemed to have purchased that power from the department.

This bill would modify the existing transmission, distribution, and related service provisions to authorize the department to contract with an electrical corporation to transmit or provide for the transmission of, and distribute all power made available by the department, and provide, as the agent of the department, billing, collection, and other related services on terms and conditions that reasonably compensate the electrical corporation for its services and adequately secure payment to the department, and would make corresponding changes to the commission's requirement to order that service at the request of the department.

(3) Existing law authorizes the department to enter into contracts for the purchase of electric power and to sell power to retail end-use customers and to local publicly owned electric utilities. Existing law requires the commission to take necessary action to ensure that all, or a portion of, the component rates that are available to electrical corporations for the purchase of their net short position of electricity are used to recover the revenue requirements for the purchase and sale functions described in this paragraph.

This bill would repeal that commission requirement.

(4) Existing law authorizes the department to issue revenue bonds for purposes described in (3) not to exceed a certain amount, containing specified terms and conditions, upon authorization by written determination of the department and with the approval of the Director of Finance and the Treasurer.

This bill would, instead, authorize the issuance of the bonds in an aggregate amount up to the greater of $13,423,000,000 or the amount calculated by multiplying by a factor of 4 the annual revenues generated by the California Procurement Adjustment; provided the aggregate amount shall not exceed $13,423,000,000. By increasing the amount of proceeds from the issuance of revenue bonds that may be expended from a continuously appropriated fund, the bill would make an appropriation.

(5) This bill would make other related clarifying and technical changes.

Appropriation: yes.

The people of the State of California do enact as follows:

SECTION 1. Section 1731 of the Public Utilities Code is amended to read:

1731. (a) The commission shall set an effective date when issuing an order or decision. The commission may set the effective date of an order or decision prior to the date of issuance of the order or decision.

(b) After any order or decision has been made by the commission, any party to the action or proceeding, or any stockholder or bondholder or other party pecuniarily interested in the public utility affected, may apply for a rehearing in respect to any matters determined in the action or proceeding and specified in the application for rehearing. The commission may grant and hold a rehearing on those matters, if in its judgment sufficient reason is made to appear. No cause of action arising out of any order or decision of the commission shall accrue in any court to any corporation or person unless the corporation or person has filed an application to the commission for a rehearing within 30 days after the date of issuance or within 10 days after the date of issuance in the case of an order issued pursuant to either Article 5 (commencing with Section 816) or Article 6 (commencing with Section 851) of Chapter 4 relating to security transactions and the transfer or encumbrance of utility property. For purposes of this article, "date of issuance" means the date when the commission mails the order or decision to the parties to the action or proceeding.

(c) No cause of action arising out of any order or decision of the commission construing, applying, or implementing the provisions of Chapter 4 of the Statutes of 2001–02 First Extraordinary Session shall accrue in any court to any corporation or person unless the corporation or person has filed an application to the commission for a rehearing within 10 days after the date of issuance of the order or decision. The commission shall issue its decision and order on rehearing within 20 days after the filing of that application.

SEC. 2. Section 1768 is added to the Public Utilities Code, to read:

1768. The following procedures shall apply to judicial review of an order or decision of the commission interpreting, implementing, or applying the provisions of Chapter 4 of the Statutes of 2001–02 First Extraordinary Session:

(a) Within 30 days after the commission issues its order or decision denying the application for a rehearing, or, if the application is granted, then within 30 days after the commission issues its decision on rehearing, any aggrieved party may petition for a writ of review in the California Supreme Court for the purpose of determining the lawfulness of the original order or decision or of the order or decision on rehearing. If the writ issues, it shall be made returnable at a time and place specified by court order and shall direct the commission to certify its record in the case to the court within the time specified. No order of the commission interpreting, implementing, or applying the provisions of Chapter 4 of the Statutes of 2001–02 First Extraordinary Session shall be subject to review in the courts of appeal.

(b) The petition for review shall be served upon the executive director of the commission either personally or by service at the office of the commission.

(c) For purposes of this section, the issuance of a decision or the granting of an application shall be construed to have occurred on the date when the commission mails the decision or grant to the parties to the action or proceeding.

(d) All actions and proceedings under this section and all actions or proceedings to which the commission or the people of the State of California are parties in which any question arises under this section, or under or concerning any order or decision of the commission under this section, shall be preferred over, and shall be heard and determined in preference to, all other civil business except election causes, irrespective of position on the calendar.

(e) The provisions of this article apply to actions under this section to the extent that those provisions are not in conflict with this section.

SEC. 3. Section 80106 of the Water Code is amended to read:

80106. (a) The department may contract with the related electrical corporation or its successor in the performance of related service, for the electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute all power made available by the

department, and, as agent of the department, provide billing, collection, and other related services on terms and conditions that reasonably compensate the electrical corporation for its services, and adequately secure payment to the department.

(b) At the request of the department, the commission shall order the related electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute all power made available by the department, and, as agent of the department, provide billing, collection, and other related services on terms and conditions that reasonably compensate the electrical corporation for its services, and adequately secure payment to the department.

SEC. 4. Section 80114 of the Water Code, as added by Chapter 4 of the Statutes of 2001, is repealed.

SEC. 5. Section 80130 of the Water Code is amended to read:

80130. The department may incur indebtedness and issue bonds as evidence thereof, provided that bonds may not be issued in an amount the debt service on which, to the extent payable from the fund, is estimated by the department to exceed the amounts estimated to be available in the fund for their payment. The department may authorize the issuance of bonds (excluding notes issued in anticipation of the issuance of bonds and retired from the proceeds of those bonds) in an aggregate amount up to the greater of thirteen billion four hundred twenty-three million dollars ($13,423,000,000) or the amount calculated by multiplying by a factor of four the annual revenues generated by the California Procurement Adjustment, as determined by the commission pursuant to Section 360.5 of the Public Utilities Code; provided, such aggregate amount shall not exceed thirteen billion four hundred twenty-three million dollars ($13,423,000,000). Nothing in this section shall prohibit the department from issuing bonds prior to the effective date of this bill based upon the authorization granted to the department by the provisions of Chapter 4 of the Statutes of 2001–02 First Extraordinary Session. Refunding of bonds to obtain a lower interest rate shall not be included in the calculation of the aggregate amount. In addition, before the issuance of bonds in a public offering, the department shall establish a mechanism to ensure that the bonds will be sold at investment grade ratings and repaid on a timely basis from pledged revenues. This mechanism may include, but is not limited to, an

agreement between the department and the commission as described in Section 80110.

SEC. 6. Section 80132 of the Water Code is amended to read:

80132. (a) Bonds may be issued by the department upon authorization by written determination of the director of the department with the approval of the Director of Finance and the State Treasurer. The Department of Finance shall notify the Chairperson of the Joint Legislative Budget Committee and the chairperson of the committee in each house that considers appropriations of its written determination. The bonds shall be sold at such prices and in such manner, and on such terms and conditions, as shall be specified in such determination, and such determination may contain or authorize any other provision, condition, or limitation not inconsistent herewith and such provisions as may be deemed reasonable and proper for the security of the bondholders. Bonds may mature at such time or times, and bear interest at such rate or rates, which may be fixed or variable and be determined by reference to an index or such other method, as shall be specified in such determination. Neither the person executing the determination to issue bonds nor any person executing bonds shall be personally liable therefor or be subject to any personal liability or accountability by reason of the issuance thereof.

(b) In the discretion of the department, any bonds may be secured by a trust agreement by and between the department and a corporate trustee, which may be any trust company or bank having trust powers within or without the state, or the State Treasurer. Notwithstanding any other provision of law, the State Treasurer shall not be deemed to have a conflict of interest by reason of acting as such trustee. The department may enter into such contracts or arrangements as it shall deem to be necessary or appropriate for the issuance and further security of the bonds.

(c) Bonds shall be legal investments for all trust funds, the funds of all insurance companies, banks both commercial and savings, trust companies, executors, administrators, trustees, and other fiduciaries, for state school funds, pension funds, and, for any funds that may be invested in county, school, or municipal bonds.

(d) Notwithstanding that bonds may be payable from a special fund, they shall be deemed to be negotiable instruments for all purposes.

(e) Any and all bonds, their transfer and the income therefrom shall at all times be free from taxation of every kind by the state and by all political subdivisions of the state.

(f) Bonds shall not be deemed to constitute a debt or liability of the state or of any political subdivision thereof, other than the department, or a pledge of the faith and credit of the state or of any such political subdivision but shall be payable solely from the funds herein provided for. All bonds shall contain a statement to the following effect: "Neither the faith and credit nor the taxing power of the State of California is pledged to the payment of the principal of or interest on this bond." The issuance of bonds shall not directly or indirectly or contingently obligate the state or any political subdivision thereof to levy or to pledge any form of taxation whatever therefor or to make any appropriation for their payment.

(g) The department may pledge or assign any revenues under any obligation entered into, and rights to receive the same, and moneys on deposit in the fund and income or revenue derived from the investment thereof, as security for the department's obligations hereunder. It is the intention of the Legislature that any pledge of moneys, revenues, or property made by the department shall be valid and binding from the time when the pledge is made; that the moneys, revenues, or property so pledged and thereafter collected from retail end use customers, or paid directly or indirectly to or for the account of the department, is hereby made, and shall immediately be, subject to the lien of such pledge without any physical delivery thereof or further act; that the lien of any such pledge shall be valid and binding as against all parties having claims of any kind in tort, contract, or otherwise against the department irrespective of whether such parties have notice thereof, and that no resolution or instrument by which such pledge or lien created pursuant to this subdivision is expressed, confirmed, or approved need be filed or recorded in order to perfect such pledge or lien. The provisions hereof shall in all respects govern the creation, perfection, priority, and enforcement of any lien created hereby or hereunder.

SEC. 7. Section 80200 of the Water Code is amended to read:

80200. (a) There is hereby established in the State Treasury the Department of Water Resources Electric Power Fund. Notwithstanding Section 13340 of the Government Code, all moneys in the fund are continuously appropriated, without regard to fiscal year, to the department, and shall be available for the purposes of this division. It is the intent of the Legislature that this fund be a continuation of the fund created in Chapter 3 of the Statutes of 2001 (SB 7 of the First 2001–02 Extraordinary Session).

(b) All revenues payable to the department under this division shall be deposited in the fund. Notwithstanding any other provision of law, interest accruing on money in the fund shall remain in the fund and shall be used for the purposes of this division. Payments from the fund may be made only for the purposes authorized by this division, including, but not limited to, payments for any of the following:

(1) The cost of electric power and transmission, scheduling, and other related expenses incurred by the department.

(2) The pooled money investment rate on funds advanced for electric power purchases prior to the receipt of payment for those purchases by the purchasing entity.

(3) Payment of any bonds or other contractual obligations authorized by this division.

(4) Repayment to the General Fund of appropriations made to the fund pursuant hereto or hereafter for purposes of this division, appropriations made to the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001. That repayment shall be made as soon as practicable.

(c) Except as provided in subdivision (b) of Section 5 of the statute adding this section, the administrative costs of the department incurred in administering this division shall be provided in the annual Budget Act.

(d) Obligations authorized by this division shall be payable solely from the fund. Neither the full faith and credit nor the taxing power of the state are or may be pledged for any payment under any obligation authorized by this division.

(e) While any obligations of the department incurred under this division remain outstanding and not fully performed or

discharged, the rights, powers, duties, and existence of the department and the commission shall not be diminished or impaired in any manner that will affect adversely the interests and rights of the holders of or parties to such obligations. The department may include this pledge and undertaking of the state in the department's obligations.

SEC. 8. Section 6 of Chapter 4 of the Statutes of 2001, First Extraordinary Session, is amended to read:

Sec. 6. (a) The Department of Finance may authorize the creation of deficiencies for the appropriation made by Section 5 of Chapter 4 of the Statutes of 2001, which added this section. No deficiency may be approved under this section any sooner than 10 days after written notification of the proposed deficiency is given to the Chairperson of the Joint Legislative Budget Committee and the chairperson of the committee in each house that considers appropriations. After November 15, 2001, such deficiency shall be limited to amounts required for short-term cash-flow purposes of no more than five hundred million dollars ($500,000,000) in the aggregate and shall be repaid from the Department of Water Resources Electric Power Fund within 180 days. The Director of Finance shall certify to the Joint Legislative Budget Committee and the Appropriations Committees as to the need for a short-term cash-flow loan not less than 10 days prior to the written notification.

(b) This section shall be repealed as of January 1, 2003, unless a later enacted statute that is enacted before January 1, 2003, deletes or extends the date on which it is repealed.

SEC. 9. The provisions of Division 27 (commencing with Section 80000) of the Water Code, including amendments made thereto in this act, and the provisions of Section 360.5 of the Public Utilities Code, are severable. If any provision of Division 27 (commencing with Section 80000) of the Water Code, including amendments made thereto in this act, or the provisions of Section 360.5 of the Public Utilities Code or application thereof, are held to be invalid, such invalidity shall not affect other provisions of either Division 27 (commencing with Section 80000) of the Water Code or the provisions of Section 360.5.

SEC. 10. No revenues of the Department of Water Resources Electric Power Fund established pursuant to Section 80200 of the Water Code may be used to pay for any undercollected amount due

to any electrical corporation or to any entity to which the amount has been assigned.

CERTIFICATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION

The California Public Utilities Commission hereby certifies that attached hereto are true and correct copies of D.01-03-009, D.01-03-081 and D.01-04-005. On April 3, 2001, the Executive Director issued D.01-04-003 modifying D.01-03-009 to correct a clerical error, and on May 14, 2001, the Commission issued D.01-05-063 denying rehearing of D.01-04-005. True and correct copies of these two decisions are attached as well. Except as so noted, D.01-03-009, D.01-03-081 and D.01-04-005 have not been amended or modified and remain in full force and effect, and the Commission acknowledges receipt of an acceptance dated June 26, 2001, of the California Department Water Resources pursuant to ordering paragraph 2 of D.01-04-005.

Dated: June 26, 2001.

CALIFORNIA PUBLIC
UTILITIES COMMISSION

By Wesley M. Franklin

Name: Wesley M. Franklin
Title: Executive Director

COM/CXW/hkr

Mailed 3/9/2001

Decision 01-03-009 March 7, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (E 3338-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
Emergency Application of Pacific Gas and Electric Company to Adopt a Rate Stabilization Plan. (U 39 E)	Application 00-11-056 (Filed November 22, 2000)
Petition of THE UTILITY REFORM NETWORK for Modification of Resolution E-3527.	Application 00-10-028 (Filed October 17, 2000) **AB X1 Implementation**

INTERIM OPINION

This order recognizes that the Water Code Section 80134 DWR revenue requirement (which includes costs of contracts for the purchase of power and related DWR indebtedness) is not subject to present or future prudency review by this Commission, and that DWR is solely responsible for setting its revenue requirement which we must include in rates.

Discussion

On February 1, 2001, Governor Davis signed Assembly Bill No. 1 from the First Extraordinary session ABX1 1 (AB X1), in an effort to alleviate the energy

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STATE OF CALIFORNIA

crisis in California. AB X1 contains many provisions necessitating action from this Commission, the Department of Water Resources (DWR), and the Department of Finance. Based on input received from parties, the Administrative Law Judge (ALJ) has adopted an expedited schedule to determine the California Procurement Adjustment (CPA) on an interim basis.

Pub. Util. Code Section 360.5, as added by AB X1, requires the Commission to calculate a CPA, which is a portion of the retail rate. The statute defines the CPA as "the difference between the generation related component of the retail rate [on January 5, 2001] and the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts and ancillary services." The statute and this Commission recognize that headroom, to be further defined under AB X1, may exist and be used to finance DWR purchases. The ALJ is now considering proposals for establishing an interim CPA and expects to render his decision on March 16, 2001. Once the interim CPA is established, we will also establish an interim allocation as required by Section 360.5. Section 360.5 mandates that we determine the amount of the CPA which is allocable to power sold by DWR. That allocation must be paid by the utilities to DWR upon receipt of revenues from retail end users. This revenue stream is denominated the Fixed Department of Water Resources Set-Aside (FDWRSA). This CPA revenue stream once established is "Fixed" because it is permanent and irrevocable.

Additionally, Water Code Section 80110 entitles DWR to recover as a revenue requirement any amounts necessary to recover monies it expends or has expended to purchase power under AB X1, as well as any other amounts

specified under Water Code Section 80134[1]. While this Commission retains its general authority under Pub. Util. Code Section 451, we specifically cannot conduct any prudency review of the DWR revenue requirement, which includes costs of contracts for the purchase of power and related DWR indebtedness. Water Code Section 80110 mandates that "any just and reasonable review under Section 451 shall be conducted and determined by the department." Therefore, we acknowledge that contracts for and purchases of power by DWR and related

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[1] Section 80134(a) declares: "The department shall, and in any obligation entered into pursuant to this division may covenant to, at least annually, and more frequently as required, establish and revise revenue requirements sufficient, together with any moneys on deposit in the fund, to provide all of the following:

(1) The amounts necessary to pay the principal of and premium, if any, and interest on all bonds as and when the same shall become due.

(2) The amounts necessary to pay for power purchased by it and to deliver it to purchasers, including the cost of electric power and transmission, scheduling, and other related expenses incurred by the department, or to make payments under any other contracts, agreements, or obligations entered into by it pursuant hereto, in the amounts and at the time the same shall become due.

(3) Reserves in such amount as may be determined by the department from time to time to be necessary or desirable.

(4) The pooled money investment rate on funds advanced for electric power purchases prior to the receipt of payment for those purchases by the purchasing entity.

(5) Repayment to the General Fund of appropriations made to the fund pursuant hereto or hereafter for purposes of this division, appropriations made to the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001.

(6) The administrative costs of the department incurred in administering this division."

indebtedness are not subject to this Commission's reasonableness review. We also acknowledge that under Section 80134(b), DWR will notify this Commission of its revenue requirement and we must ensure its receipt.[2]

Water Code Section 80114 requires the Commission to ensure that "all, or a portion of, the component rates that are available to the electrical corporations for the purchase of their net short position of electricity are used to recover the revenue requirements" that DWR sets. We acknowledge that this means that this net short stream of income is totally within the control of DWR, is not subject to any prudency review by this Commission, must be paid to DWR and is therefore irrevocably DWR's money.

The exact amount of the net short revenue stream as it relates to the CPA calculation and allocation is still under consideration by this Commission. DWR itself has yet to set a revenue requirement and notify us of it. However, DWR has notified this Commission of the need for these assurances by its February 16, 2001 letter, which is Attachment A. The letter states that Commission action is necessary in order to negotiate favorable terms with sellers of power and to also provide assurances to prospective lenders of DWR's ability to recover revenues from the sale of power to retail end use customers. Water Code Section 80003(a) notes the DWR purchasing program is an essential governmental purpose. Section 80003(b) states that the provisions added by AB X1 "shall be construed in a manner so as to effectuate the purposes and objectives thereof." Water Code Section 80016 directs all state agencies to give DWR reasonable assistance or other cooperation in carrying out the purposes of AB X1. It is our duty to

[2] We recognize that Section 80110 provides some rate increase relief to a portion of residential ratepayer usage, but it in no way alters the fact the monies are due DWR.

facilitate DWR's purchases of power so it may carry out its responsibilities under AB X1. Therefore, we believe it appropriate to provide these assurances.

It is our intent to establish an interim CPA and interim allocation as soon as possible consistent with due process. At that time we will segregate revenues as requested by DWR. However, the DWR may recover, and the Commission shall approve and impose, either as part of the CPA or as additional rates, rates sufficient to enable DWR to recover its revenue requirements on a timely basis and the provisions of this sentence shall constitute an agreement within the meaning of Section 80110.

Finally, due to pending legislation which would alter Section 80110, we shall stay action on implementation of the suspension of direct access under Water Code Section 80110 until further order.

Comments on Decision

Pub. Util. Code Section 311(e) provides for public review and comment; however, this period may be reduced under certain circumstances. Under Rule 77.7(f)(9) of its Rules of Practice and Procedure, the Commission may determine on its own motion that public necessity requires reduction of this 14-day period. We have weighed the interest in allowing the full comment period against the need to provide certainty about our implementation of these aspects of AB X1, and conclude that the public interest in providing certainty at an early date, especially in the current energy crisis, outweighs the interest in allowing a full comment period. Therefore, this period was reduced.

Comments were filed on March 2, 2001 by Pacific Gas and Electric Company (PG&E), Southern California Edison Company (Edison), San Diego Gas & Electric Company (SDG&E), the Coalition of California Utility Employees (CCUE), the Alliance for Retail Energy Markets (AReM), the Aglet Consumer

Alliance (Aglet) and Enron Power Marketing, Inc. (Enron).[3] Reply comments were filed by AReM and Aglet on March 5, 2001.

PG&E requests two modifications. First, PG&E asks that the Commission require DWR to purchase the full net short open position of the utilities as a condition precedent to the utilities' obligation to remit payment to DWR for its power procurement. Second, PG&E asserts that the conclusion of law and ordering paragraph, which find that an agreement within the meaning of Water Code Section 80110 exists, should be modified. It requests that the Commission state that the agreement is interim and subject to refund until DWR's final revenue requirement is set under Section 80110, and that it is limited to the recovery of DWR's revenue requirement and does not include the CPA allocation under Pub. Util. Code Section 360.5.

Edison supports this decision. However, it requests that the Commission call on DWR to purchase the full net short position of the utilities pursuant to the legislative intent of AB X1.

SDG&E supports the decision's approach to await an interim CPA determination under ALJ DeUlloa's expedited schedule before allocating revenues to DWR. However, SDG&E asserts that the decision should contain more findings of fact and conclusions of law reflecting its discussion and, similarly, that an additional ordering paragraph should be included. Like PG&E, SDG&E calls for conditioning DWR's receipt of revenue from SDG&E upon DWR's purchase of all of SDG&E's net short position. SDG&E also objects to characterizing the assurance as to DWR's right to recover rates sufficient to enable DWR to recover its revenue requirements as an agreement under Section

[3] Enron's March 2 motion to intervene and become a party is granted.

80110. Finally, SDG&E believes that the Commission should specify its rationale for staying action on suspension on direct access, speculating that it relates to pending legislation on the topic.

Aglet contends that the references to "net short stream of income" and "net short revenue stream" are inaccurate. Aglet believes that such references imply that these revenues might cover the entire net short position of the utilities. It asserts that such coverage is unclear at this time and therefore the Commission should use the term "available net short revenues".

On March 5, 2001, DWR has forwarded a letter to the Commissioners stating its support for this decision. A copy of the letter is appended as Attachment B. DWR declares that the present needs of DWR are satisfied by this decision and requests its adoption at the March 7, 2001 Commission meeting.

While we believe that PG&E, SDG&E and Edison raise valid concerns over the legislative intent of AB X1, we will not call for DWR to purchase the entire net short position of the utilities. This Commission has no jurisdiction over DWR's purchasing decisions. For this reason we also decline to make DWR's purchase of the entire net short position a condition precedent to the utilities' obligation to remit funds to DWR. We also reject the changes requested by PG&E and SDG&E as to our declaration of the existence of an agreement under Water Code Section 80110. We find that further findings of fact, conclusions of law or ordering paragraphs, as urged by SDG&E, are unnecessary. We reject Aglet's assertion that our nomenclature as to net short revenues is inaccurate.

Enron asserts that this decision is the appropriate response to the DWR letter of February 16, 2001. While this decision does not require the utilities to enter into agreements with DWR for distribution and billing of and payment for

power, Enron believes such a request is premature. Enron contends that such an order is not needed at this time because there is no record that DWR has encountered problems in contracting with the utilities for these functions.

CCUE contends that direct access is inconsistent with the procurement structure of AB X1 because it would allow switching to non-utility providers in order to avoid payment of a fair share of DWR costs when the price of power falls below the DWR price in the future. It asserts that customers should not be able to flee to take advantage of lower prices when that time comes. CCUE believes the Commission should end the cycle to direct access providers entering the market when times are good and dumping their customers on the utilities when times are bad. Therefore, CCUE believes that the Commission should pursue a directive to suspend direct access under Water Code Section 80110 as expeditiously as possible.

AReM supports the stay of implementation of AB X1's suspension of direct access. It observes that the Legislature is considering modification of the Water Code Section 80110 suspension. AReM also notes that DWR's letter does not request such action. It asserts that the Commission can avoid the creation of new stranded costs without infringing on customer choice. AReM believes that there is no need to rush to judgment on the suspension of direct access since Section 80110 does not place a time constraint on the Commission regarding its implementation.

We do not find that a stay of implementation of AB X1's suspension of direct access is necessary at this time.

We have made other nonsubstantive changes.

Findings of Fact

1. On February 1, 2001, Governor Davis signed AB X1 in an effort to alleviate the energy crisis in California.

2. Pub. Util. Code Section 360.5, as added by AB X1, requires the Commission to calculate a CPA, which is a portion of the retail rate.

3. The statute and this Commission recognize that headroom, to be further defined under AB X1, may exist and be used to finance DWR purchases.

4. Water Code Section 80110 mandates that "any just and reasonable review under Section 451 shall be conducted and determined by the department."

5. Water Code Section 80114 requires the Commission to ensure that "all, or a portion of, the component rates that are available to the electrical corporations for the purchase of their net short position of electricity are used to recover the revenue requirements" that DWR sets.

6. DWR has notified this Commission of the need for these assurances by its February 16, 2001 letter, which is Attachment A. The letter states that Commission action is necessary in order to negotiate favorable terms with sellers of power and to also provide assurances to prospective lenders of DWR's ability to recover revenues from the sale of power to retail end use customers. By letter dated March 5, 2001 (Attachment B), DWR states that this decision meets its present needs.

7. Under Rule 77.7(f)(9) of its Rules of Practice and Procedure, the Commission may determine on its own motion that public necessity requires reduction of the public review and comment period.

8. We have weighed the interests in allowing the full comment period against the need to provide certainty about our implementation of these aspects of AB X1, and determined that the balance favors providing certainty at this time.

Conclusions of Law

1. Section 360.5 mandates that we determine the amount of the CPA which is allocable to power sold by DWR. That allocation must be paid by the utilities to DWR upon receipt of revenues from retail end users.

2. Contracts for and purchases of power by DWR and related DWR indebtedness are not subject to this Commission's reasonableness review.

3. Under Section 80134(b), DWR will notify this Commission of its revenue requirement and we must ensure its receipt.

4. Water Code Section 80114 means that this net short stream of income is totally within the control of DWR, is not subject to any prudency review by this Commission, must be paid to DWR and is therefore irrevocably DWR's money.

5. The Commission must facilitate DWR's purchases of power so it may carry out its responsibilities under AB X1. Therefore, we believe it appropriate to provide these assurances.

6. DWR may recover, and the Commission shall approve and impose, either as part of the CPA or as additional rates, rates sufficient to enable DWR to recover its revenue requirements on a timely basis and the provisions of this sentence shall constitute an agreement within the meaning of Section 80110.

7. Due to the need for DWR to enter into contracts pursuant to AB X1, we conclude that the public interest in providing certainty about our implementation of certain aspects of AB X1 outweighs the interest in allowing a full comment period; therefore, this period was reduced.

INTERIM ORDER

IT IS ORDERED that the Department of Water Resources (DWR) may recover, and the Commission shall approve and impose, either as part of the

California Procurement Adjustment or as additional rates, rates sufficient to enable DWR to recover its revenue requirements on a timely basis and the provisions of this sentence shall constitute an agreement within the meaning of Section 80110.

This order is effective today.

Dated March 7, 2001, at San Francisco, California.

LORETTA M. LYNCH
President
RICHARD A. BILAS
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners

We will file a joint concurrence.

/s/ LORETTA M. LYNCH
President
/s/ CARL W. WOOD
Commissioner

I will file a concurrence.

/s/ RICHARD A. BILAS
Commissioner

I will file a dissent.

/s/ HENRY M. DUQUE
Commissioner

ATTACHMENT A

[Letterhead of Department of Water Resources]

February 16, 2001

Commissioners
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Dear Commissioners:

As you are aware, pursuant to recently enacted provisions of the Water Code, the Department of Water Resources (the "Department") is authorized to contract for the purchase of power for sale to retail end use customers within the State of California at such prices and on such terms and conditions as the Department determines appropriate. The Department has begun to enter into contracts for the purchase of power ("Power Purchase Contracts") in accordance with such provisions and pursuant to the Proclamation of Governor Gray Davis dated January 17, 2001 concerning shortages of electricity.

In order to induce the sellers of power to enter into such Power Purchase Contracts on favorable terms to the State and to provide assurances to prospective lenders to the Department as to the ability of the Department to recover its revenue requirement, it is critical that the Commission begin to implement the provisions of AB 1X so that the Department will realize at least a portion of its current revenue requirements from the sale of power to retail end use customers.

The power being purchased by the Department has been and is being delivered to retail end use customers. Revenues relating to such power, which pursuant to the Water Code are the property of the Department, have been or will very shortly begin to be collected by the electrical corporations. Such revenues, of course, are a critical source of funding for the power purchases being made and reimbursing the State for moneys appropriated to the Department to fund such purchases. In order to assure that the Department's revenues are properly segregated and accounted for and promptly remitted to the Department and to minimize the continuing need for General Fund appropriations, it is critical that the Commission at the earliest possible

opportunity adopt an appropriate emergency order addressing several matters discussed below.

Pursuant to Section 80110 of the Water Code, the Department is entitled to recover as a revenue requirement amounts necessary to enable the Department to, among other things, pay for the power purchased by it, and to make payments under any contracts, agreements and obligations entered into by the Department in the amounts and at the times the same become due. Under the terms of said Section 80110, any "just and reasonable" review under Section 451 is to be conducted by the Department and not by the Commission.

As part of an emergency order, the Department requests that the Commission confirm the Department's understanding that charges for power delivered to retail end use customers will provide sufficient revenues, together with other moneys available to the Department within the Department of Water Resources Electric Power Fund for such purpose, to meet the entire revenue requirement of the Department under Section 80110, including all payments made on or after January 17, 2001 by the Department under Power Purchase Contracts entered into by the Department and determined by the Department to be just and reasonable.

The Department also requests that such emergency order establish an interim method of allocating current generation charges paid by retail end use customers in order to assure a current recovery by the Department of a portion of its ongoing costs. We recognize that any interim allocation of such charges may be adjusted in accordance with subsequent Commission action and that the rates and charges for Department power will ultimately be established pursuant to a further agreement with the Department, all in accordance with relevant provisions of the Water Code. However, it is critical to the success of the Department's power purchasing program that an initial allocation of revenues be made and that appropriate collection provisions be immediately implemented.

We also request that such order require the electrical corporations to (i) transmit and distribute the Department's power, (ii) provide billing and collection services for the Department, (iii) segregate in a separate account and hold in trust for the Department all revenues allocable to the Department's power as received, and (iv) remit such revenues to the Department upon receipt. We also request that the electrical corporations be directed to enter into servicing agreements with the Department to implement the foregoing.

In addition, we request that the order provide that, upon its acceptance by the Department, the order will constitute an agreement between the Department and the Commission within the meaning of Section 80110 of the Water Code.

Thank you for your assistance and attention to this important matter. We will be submitting additional information and requests to the Commission relating to the Department's power purchase program and financing plans and appreciate your continuing cooperation.

Sincerely,

/s/ Raymond D. Hart

for Thomas M. Hannigan
Director

(END OF ATTACHMENT A)

ATTACHMENT B

March 5, 2001

Commissioners
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Re: Draft Decision of Commissioner Bilas Relating to Powers of the Department of Water Resources and the Interim Allocation of Electricity Revenues

Dear Commissioners:

In a letter to you dated February 16, 2001, the Department of Water Resources (the "Department") requested that the Commission confirm the Department's understanding that charges for power delivered to retail end use customers will provide sufficient revenues, together with other moneys available to the Department within the Department of Water Resources Electric Power Fund for such purpose, to meet the entire revenue requirement of the Department under Section 80110 of the Water Code.

We wish to reaffirm the statements made in the letter of February 16th and to also inform you that the Department is currently in the process of obtaining interim financing for all or a portion of its power purchase costs.

While we initially supported Item 3 and there are aspects of both of the Draft Decisions before the Commission on this subject that are helpful in terms of ensuring that the revenue requirements of the Department are met, upon further consideration the Department believes the specific language of the Draft Decision of Commissioner Bilas would satisfy the Department's needs at this time. Therefore, in order to enable the Department to expeditiously implement the program described in Assembly Bill 1x, the Department requests that the Commission adopt the Draft Decision of Commissioner Bilas at its March 7th meeting. We understand that this decision is one of several that the Commission will be addressing on the issue of the allocation of revenues to the Department and that future decisions will refine this allocation process.

Thank you for your assistance and attention to this important matter. We will be submitting additional information and requests to the Commission relating to the Department's power purchase program and financing plans and appreciate your continuing cooperation.

Sincerely,

/s/ Raymond D. Hart

for Thomas M. Hannigan
Director

(END OF ATTACHMENT B)

Commissioner Richard A. Bilas, concurring:

Though I am pleased that today's decision meets Department of Water Resource's (DWR) current needs and permits us to proceed on a determination of a California Procurement Adjustment consistent with due process, I am disappointed that two key provisions of my proposed order were not adopted.

First, we should resolve the issue of whether DWR should be buying all net short power needs for the three utilities. I recognize that we have no jurisdiction over DWR's purchasing decisions. I appreciate DWR's need to exercise care in making purchasing decisions since DWR's revenue requirement is not subject to our reasonableness review and must be included in rates. However, my interpretation of the legislative intent behind AB X1 is that the bill was meant to eliminate further additions to the utilities' undercollections by having DWR cover all net short electricity needs of the utilities. That is the intent espoused by the bill's author, Assemblymember Keeley, and in the Assembly Floor Analysis of the bill. That analysis states, "the IOUs are still 'net short' with regard to generation. The net short is the electricity needs of customers that are not met by the generation resources owned or under contract to the utilities. This bill requires DWR to cover the 'full net short' of the IOUs, and to a limited extent, the net short of municipal utilities." (Analysis at 8.) At present the California Independent System Operator (ISO) is still making costly last minute purchases of power, and the issue of who is responsible for payment is unresolved. This uncertainty adds to the utilities' financial distress and must be resolved somewhere and soon. I believe the Commission should urge an end to these ISO purchases by calling on DWR to purchase the entire net short electricity position of the utilities under DWR's AB X1 authority, just as I believe we must raise rates to make AB X1 workable.

I also believe that a stay of implementation of AB X1's suspension of direct access is the most appropriate course at this time. The prudent course is to await the Legislature's adoption of its final position regarding direct access before proceeding under Water Code Section 80110. We should take official notice of Senate Bill (SB) X1 27 (Bowen) and SBX1 18 (Escutia) which may result in changes to the suspension of direct access. I also concur with AReM's comments on my alternate decision that AB X1 sets no time limit on the Commission's consideration of the suspension. Direct access is not a discredited concept. Had it been allowed to flourish, the State might not be in the present crisis situation. Choice and innovation must not be stifled by destroying all remnants of direct access in the name of a central planning ideology.

/s/ RICHARD A. BILAS
RICHARD A. BILAS
Commissioner

San Francisco, California
March 7, 2001

Commissioner Henry M. Duque, dissenting:

Today's decision partially recognizes the Water Code sections under Assembly Bill 1X which speak to the needs of the Department of Water Resources. In particular, it recognizes that the revenue requirement of the Department of Water Resources is 1) not subject to reasonableness review (section 80134), 2) is fully recoverable (80110, 80114, and 80134), and 3) is guaranteed. While I fully support these efforts, I cannot ignore what the final decision does not address.

I am filing today's dissent because the final decision 1) did not address the need for the Department of Water Resources to cover all the net short electricity needs of the utilities, and 2) eliminated the language which would have this Commission recognize pending legislation on direct access.

While some Commissioners are now suggesting that the direct access language should never have been incorporated in the draft order, the fact remains that the language and message was out there in the proposed item 3 on the Commission's February 22 agenda. Although the mere deletion and references to the Commission's position on direct access seems like a reasonable action, I cannot ignore the public statements of fellow Commissioners at today's meeting. If what I heard today was true, some would believe that the Commission should take the opportunity to stop retail competition before the legislature acts because Assembly Bill 1X gives us the authority to do so. I strongly disagree. I await the pending legislation that will address direct access directly and I await the clean up bill to Assembly Bill 1X.

Finally, the reluctance of this Commission to expressly state a recognition of DWR's responsibility for the net short position is yet another lapse in our public duty. The author of AB 1X himself agrees that this was the intent of the legislation. It is important that this Commission be cognizant of the solvency of the utilities, and be responsive to the recovery of DWR's costs. Inadvertent or purposeful attempts to confuse the intent of the legislation is just plain wrong and I cannot support that effort.

For these reasons, I must note my dissatisfaction with today's decision and respectfully dissent.

/s/ HENRY M. DUQUE
Henry M. Duque
Commissioner

March 7, 2001

San Francisco

Mailed 4/3/2001

ALJ/LTC/t94

Decision 01-04-003 April 3, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (E 3338-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
Emergency Application of Pacific Gas and Electric Company to Adopt a Rate Stabilization Plan. (U 39 E)	Application 00-11-056 (Filed November 22, 2000)
Petition of THE UTILITY REFORM NETWORK for Modification of Resolution E-3527.	Application 00-10-028 (Filed October 17, 2000) AB X1 Implementation

ORDER CORRECTING ERROR

The Commission is aware of an inadvertent error in the final production of Decision (D.) 01-03-009 and will correct that error in this order. The error occurred as the Commission was preparing the adopted decision for mailing on March 9, 2001. At that time, the Commission failed to completely incorporate all revisions required to reflect its approval of Commissioner Wood's alternate pages, which removed references in agenda item 3a to staying action on implementation of suspension of direct access under Water Code Section 80110. This deletion was made elsewhere in D.01-03-009, but was inadvertently overlooked in the text of the second full paragraph on page 5. The text in question reads as follows:

Certified as a True Copy of the Original
Wesley M. Franklin
EXECUTIVE DIRECTOR, PUBLIC UTILITIES COMMISSION
STATE OF CALIFORNIA

"Finally, due to pending legislation which would alter Section 80110, we shall stay action on implementation of the suspension of direct access under Water Code Section 80110 until further order. "

Therefore, pursuant to the authority granted in Resolution A-4661, **IT IS ORDERED** that the second full paragraph on mimeo. page 5 of Decision 01-03-009, recited above, is deleted.

This order is effective today.

Dated April 3, 2001, at San Francisco, California.

/w/ WESLEY M. FRANKLIN

WESLEY M. FRANKLIN
Executive Director

CERTIFICATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION

The California Public Utilities Commission hereby certifies that attached hereto are true and correct copies of D.01-03-009, D.01-03-081 and D.01-04-005. On April 3, 2001, the Executive Director issued D.01-04-003 modifying D.01-03-009 to correct a clerical error, and on May 14, 2001, the Commission issued D.01-05-063 denying rehearing of D.01-04-005. True and correct copies of these two decisions are attached as well. Except as so noted, D.01-03-009, D.01-03-081 and D.01-04-005 have not been amended or modified and remain in full force and effect, and the Commission acknowledges receipt of an acceptance dated June 26, 2001, of the California Department Water Resources pursuant to ordering paragraph 2 of D.01-04-005.

Dated: June 26, 2001.

CALIFORNIA PUBLIC
UTILITIES COMMISSION

By Wesley M. Franklin

Name: Wesley M. Franklin
Title: Executive Director

COM/LYN/sid

Mailed 3/27/2001

Decision 01-03-081 March 27, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (E 338-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
Emergency Application of Pacific Gas and Electric Company to Adopt a Rate Stabilization Plan. (U 39 E)	Application 00-11-056 (Filed November 22, 2000)
Petition of THE UTILITY REFORM NETWORK for Modification of Resolution E-3527.	Application 00-10-028 (Filed October 17, 2000) **AB 1X**

INTERIM OPINION

I. Summary

This order implements legislation allowing the state to provide electricity that its utilities are unable to provide. First, this order requires utilities to provide the Department of Water Resources with the money they have collected, that was earned by the sale of power paid for by the Department of Water Resources. Currently, both utilities and the Department of Water Resources sell power to end use customers, but the utilities collect revenues in lump sum for all power that is delivered. Second, this order sets out a proposed method the Commission will use to calculate the "CPA," the California Procurement Adjustment established by Public Utilities Code Section 360.5.[1] This order then

[1] CPA amounts will be used to determine the amount of the bonds the Department of Water Resources can issue to support its power purchases. In addition, the Commission may order that a portion of the revenues generated by the CPA be paid to DWR as partial reimbursement for its power purchases. That portion is the "Fixed DWR Set-Aside."

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STATE OF CALIFORNIA

applies this proposed method, and calculates—for each utility—a proposed company-wide average CPA rate. Using that rate, this order determines a proposed CPA revenue amount, which can be used by the Department of Water Resources to begin the process of issuing bonds. Following a discussion of the context in which this decision is issued, we take these actions in Sections VI, VII and VIII, below.

II. Background

On February 1, 2001, Assembly Bill (AB) 1 from the First Extraordinary Session (AB 1X) was signed into law. Wholesale energy prices that had soared to unprecedented levels had caused a deterioration in Southern California Edison Company's (Edison) and Pacific Gas & Electric Company's (PG&E) financial condition, leaving them unable to buy all the power needed to serve their customers. In response to this emergency situation, AB 1X authorizes DWR to purchase electric power for AB 1X sale directly to retail end-use customers[2] being served by utilities.[3] When these customers take delivery of DWR's power, they are deemed to have purchased it. DWR power is to be allocated for delivery to all classes of retail end-use customers on a pro rata basis, to the extent possible.[4]

AB 1X contains a number of mechanisms to pay DWR for the electricity it sells. Several are relevant here. Section 2 of AB 1X adds Section 360.5 to the Public Utilities Code. Section 360.5 contains detailed requirements for the calculation of an amount know as the "California Procurement Adjustment" or "CPA." That statute provides:

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[2] Water Code Section 80002.5.

[3] In this decision, we use the term "utilities" interchangeably with "electrical corporations".

[4] Water Code Section 80002.5.

> "The commission shall determine that portion of each existing electrical corporation's retail rate effective on January 5, 2001, that is equal to the difference between the generation related component of the retail rate and the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services. That portion of the retail rate shall be known as the California Procurement Adjustment. The commission shall further determine the amount of the California Procurement Adjustment that is allocable to the power sold by the department. That amount shall be payable, by each electrical corporation, upon receipt by the electrical corporation of the revenues from its retail end use customers, to the department for deposit in the Department of Water Resources Electric Power Fund, established by Section 80200 of the Water Code. The amount determined pursuant to this subdivision shall be known as the Fixed Department of Water Resources Set-Aside."

AB 1X also establishes the DWR Electric Power Fund (the "Fund") in the State Treasury, and authorizes DWR to issue bonds, notes, and other evidences of indebtedness (collectively, "Bonds") for certain limited purposes, including:

- paying the costs of electric power and transmission, scheduling, and other related expenses, or to reimburse expenditures from the Fund for those purposes.

- repaying to the General Fund certain advances made to DWR for the power purchase program; and

- establishing or maintaining reserves in connection with the Bonds and paying certain costs incidental to the issuance, payment and security of the Bonds.

Water Code Section 80130, enacted as part of AB 1X, addresses the issuance of bonds by DWR to finance electricity purchases. That statute provides in relevant part:

> "In no event shall the [DWR] authorize the issuance of bonds ... in an aggregate amount greater than the amount calculated by multiplying by a factor of four the annual revenues generated by the California Procurement Adjustment, as determined by the commission pursuant to Section 360.5."

III. Procedural History

On February 5, 2001, Administrative Law Judge (ALJ) Joseph DeUlloa issued a ruling setting a prehearing conference on February 6, 2001, to discuss the requirements of the Department of Finance for implementing AB 1X. The ALJ ruling also set workshops[5] on February 6 and 7 for the implementation of AB 1X and a second prehearing conference on February 7 to discuss workshop progress.

Initially, the utilities proposed to submit advice letters that would take effect on the day submitted to the Commission. The ALJ rejected this approach and issued a ruling directing the utilities to serve their proposals for determining CPA. The ruling also provided parties an opportunity to comment on the proposals for determining CPA. The issues we decide are not predicated on factual disputes. Rather, the issues we decide are interpretations of law. Although a trial-type evidentiary hearing has not been held, parties have been afforded an opportunity to be heard through written comment on the utilities' proposals, and comments on DWR's letter. Further, parties will have an opportunity to submit comments on the proposal contained in this order. In short, there will have been a fair hearing.

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[5] The following attended these workshops: PG&E, Edison, San Diego Gas & Electric Company (SDG&E), Office of Ratepayers Advocates, Department of Water Resources (present only on the first day of workshop), The Utility Reform Network, ENRON Energy Services, AES New Energy, Inc., CLECA, Calpine Corporation, Federal Executive Agencies, Aglet Consumer Alliance, CMTA, Turlock Irrigation District, Watson Cogeneration Company, IEP, California Farm Bureau Federation, New West Energy, Cal-Pine CAL-SLA, Pacificorp, Dynergy, CAC/ EPUC, and JDRP.

On February 23, 2001, Edison, PG&E, and SDG&E each served a proposal to calculate the CPA on a monthly basis by subtracting generation-related costs from generation-related revenues. Each proposed to calculate generation-related revenue residually from the total retail rate and also adjust revenues for certain costs. Each utility's proposal for calculating CPA differs in the inputs used in its calculation. Further, all three, in effect, propose to create balancing accounts for tracking CPA on a monthly basis.

The Office of Ratepayer Advocates (ORA), Aglet Consumer Alliance (Aglet), and Enron Energy Services, Inc. (Enron) either challenge some of the adjustments made in calculating generation-related revenues and / or also challenge some of the expenses the utilities include in generation-related costs. Greenlining Institute and Latino Issues Forum request that the Commission exempt CARE eligible customers from the CPA. TURN offered more extensive comment and advocates that the Commission also consider other aspects of AB 1X in adopting a CPA, such as freezing rates for residential usage up to 130% of baseline, and reject the utilities' balancing account approach. Further, TURN also challenges the adjustments to revenue, and generation costs identified by the utilities.

IV. DWR's Request

In a letter to the Commission dated March 14, 2001, DWR set forth its views on how the Commission should determine the CPA. (See Attachment A.) This letter was provided the parties for comment by ALJ ruling.

DWR believes the Commission's determination of the CPA is a critical element in the implementation of AB 1X and the initial step in establishing a revenue source for DWR in meeting its power purchase responsibilities. Further, DWR asserts that the CPA is also important to any long-term or short-term

financing. Based on the comments received from parties, we agree with DWR's characterization of the importance of the CPA.

DWR argues that nothing in AB 1X suggests that the utilities should retain any revenues attributable to power furnished by DWR. DWR believes Section 360.5 contemplates that utilities will no longer bear costs for the "net short" power that DWR buys in their place, and that utility generation rates should be adjusted to reflect DWR's purchases. DWR asserts that Section 360.5 was also intended to provide financial assurance to DWR for its power purchases.

In general summary, DWR believes that for the sale of net short energy to the customers of each utility, *DWR* should receive:

(i) a per-kWh price equal to the applicable generation-related retail rate per kilowatt-hour established for each utility as in effect on January 5, 2001; plus

(ii) a Commission-determined portion of the January 5, 2001 rate for power the utility continues to sell. (Fixed DWR Set-Aside.)

Further, *each utility*, on a per-kWh basis, should receive:

(i) the components of the January 5, 2001 rate attributed at the time of original rate-making to power that the corporation will continue to sell to its retail end use customers, (*i.e.*, native generation, qualifying facility contracts, existing bilateral contracts and ancillary services); plus

(ii) a portion of the January 5, 2001 rate for power the electrical corporation continues to sell, to be determined by the Commission, (*i.e.*, the portion of such rate which is not determined to be part of the Fixed DWR Set-Aside.)

Specifically, for each utility, DWR believes the Commission should do the following:

> First: Identify the generation related component of the corporation's retail rate that was in effect on January 5, 2001, expressed in terms of cents per kilowatt-hour (the "Total Generation Related Rate").
>
> Second: Determine the "sum of the costs" (also expressed as a rate, *i.e.*, in terms of cents per kilowatt-hour) imputed by the Commission to the corporation's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services at the time the January 5, 2001 rate was established (the "Utility Retained Rate").
>
> Third: Determine "the difference between" the Total Generation Related Rate and the Utility Retained Rate. That is, subtract the Utility Retained Rate from the Total Generation Related Rate to determine the CPA applicable to the utility.

For power *sold by the utility,*[6] DWR asserts that each utility must pay DWR an amount equal to the product of (i) the number of kilowatt-hours purchased by retail end users from the utility, multiplied by (ii) the Fixed DWR Set-Aside.[7] DWR asserts that such payment is due upon the utility's receipt of payment by each of its retail end-use customers.

DWR also makes a number of points about the nature of the CPA. DWR asserts that the CPA is a set, immutable rate, which should be expressed in terms of cents per kilowatt-hour. DWR contends that any changes in the costs of any generation resource of any utility from the costs reflected in the January 5, 2001 rate should not affect the CPA. .

DWR's letter asserts that the calculation of the CPA does not alter DWR's right to recover any portion of its revenue requirement, which AB 1X does not require to be fully recovered through the Fixed DWR Set-Aside. Similarly,

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[6] As opposed to power deemed sold to an end user by the DWR.

[7] DWR's letter does not request a determination of the Fixed DWR Set-Aside.

calculation of the CPA does not prevent the Commission from allowing utilities to recover their costs for that portion of the power for which they remain responsible. Further, DWR believes that the calculation of the CPA does not per se determine the division of the CPA as between DWR (Fixed DWR Set Aside) and any utility. DWR requests that the Commission determine the CPA now, and the Fixed DWR Set Aside at a later date.

Finally, DWR makes specific requests of the Commission. It requests that the Commission (i) determine, pursuant to Section 360.5, the CPA of each utility, and (ii) acknowledge that DWR may rely upon this determination for the purposes of Water Code Section 80130. Lastly, DWR requests that upon DWR's acceptance of this order in writing, that it constitute an agreement between DWR and the Commission having the full force and effect of a financing order, as provided by Water Code Section 80110.

V. Positions of Parties With Respect to Methodology for Calculating the CPA

In its initial proposal, Edison proposes to calculate the CPA on a monthly basis by subtracting recorded generation-related costs from generation-related revenues. Edison will send the amount by which revenues exceed costs to DWR only if no deficits exist from prior months. If revenues are less than costs, Edison proposes to create and record this deficit in a CPA Balancing Account.

Edison contends that DWR's proposal to receive a portion of Edison's generation revenues is inconsistent with Public Utilities Code Section 360.5 and should be rejected. However, Edison believes that DWR's proposed calculation of the CPA has merit if the Commission makes some adjustments. In any case, Edison argues that a rate increase is needed to ensure that Edison, Qualifying Facilities (QFs) and DWR have sufficient funds to provide power. Edison asserts that the Commission should immediately declare an end to the rate freeze and

raise retail rates. Edison's March 21, 2001 filing, in response to the DWR letter, calculates that the CPA is negative, using DWR's methodology (Appendix A). Edison calculates that a 60.84% increase in the total rate level is needed if DWR's methodology is used (Appendix B).

Edison also contends that AB 1X provides that Edison must be made whole for the generation it provides through existing contracts and retained generation. Edison proposes that the Commission accomplish the goal of making both it and DWR whole for the costs they each incur in procuring power for Edison's customers by adopting three separate, dedicated rate components with associated balancing accounts. These three rate components would be Edison Retained Generation, Edison Contracts, and DWR Contracts.

An initial amount would be established for these components based on an estimate of costs for each component for the next 12 months. The revenues collected from those components along with their associated costs would be tracked in a balancing account. At regular intervals, based on the extent of the amounts over- or under-collected, rate components would be adjusted. In addition, the annual forecasts would be reviewed and adjusted where necessary in the Annual Revenue Adjustment Proceeding (RAP).

PG&E proposes to calculate the CPA in a two-step process. First, PG&E would subtract its costs and other adjustments from its gross generation revenues to determine the generation-related component of its revenues. Second, PG&E would subtract its generation-related costs to determine the CPA. PG&E proposes to provide the CPA to DWR, if revenues exceed costs.

PG&E believes that DWR reads more into AB 1X than the plain language of the statute allows, by claiming an unlawful entitlement to a portion of the revenues recoverable by PG&E for utility service, which would result in an unconstitutional taking. In addition, PG&E asserts that DWR's proposal would

build into PG&E's current rates a continuing shortfall, leaving it without sufficient revenues from the generation component of rates to pay the generation-related costs specified by AB 1X. This would cause PG&E's power suppliers to refuse to sell to it. Like Edison, PG&E proposes that the Commission declare an end to the rate freeze and increase rates.

SDG&E similarly proposes to subtract costs from generation-related revenue to calculate the CPA. SDG&E also proposes to carry over negative amounts to future months for future collection.

SDG&E believes that the Commission cannot implement DWR's CPA proposal because DWR's methodology is based on misunderstandings of fundamental ratemaking concepts (*e.g.*, confusing adopted rates and actual costs). Further, SDG&E asserts that DWR has misread the law and reached erroneous conclusions, such as its belief that the CPA can never be negative, that the CPA should be calculated as a rate instead of a dollar amount, and that the CPA cannot change. SDG&E asks the Commission to carefully review DWR's proposal and to adopt a CPA calculation which is consistent with the law and ratemaking practices, is logical, and is capable of being implemented quickly.

Various parties including Aglet, TURN and ORA disputed the numerous specifics of the utilities claims. In sum, pleadings indicate that the utilities' proposal must be closely scrutinized.

VI. Discussion

A. Statutory Principles

In theory, the statutory methodology for determining the CPA is — for the most part — straightforward. The generation-related component of retail rates minus specific utility generation-related costs equals the CPA. In practice, details such as subtracting a "cost" from a "rate" pose challenges. In addition, it is important to keep in mind the entire mechanism adopted in AB 1X. TURN's

and Aglet's point that the statute must be read as a whole is well taken. The utilities' proposals, for example, inject certain views concerning the "intent" of statutory provisions that cannot be supported when the statute is read as a whole.

Prior to addressing the determination of the CPA, we must address the utilities' misconception that the fixed DWR Set-Aside portion of the CPA is the only source of revenue that may flow to DWR.[8] Section 360.5 contains no such limitation; rather, it sets forth a formula for determining a rate element known as the CPA. Nothing in the plain language of Section 360.5 says that the Fixed DWR Set-Aside portion of CPA is the only revenue stream that flows to DWR.[9] On the contrary, as discussed below, DWR is entitled by law to an amount equal to the number of kWhs sold to end-use customers multiplied by the relevant generation rate.

We must implement Section 360.5 in view of other changes imposed by AB 1X. We note that DWR's procurement of power improves the financial stability of SDG&E, PG&E and Edison.[10] Without DWR's actions, the utilities' financial situations would have continued to deteriorate. Instead, AB 1X has

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[8] Edison states: "CPA ... sets forth the amount that California's Investor-Owned Utilities (IOUs) have available in revenues to send to [DWR]." Edison's February 23, 2001, Proposal for an Interim CPA (entitled "Testimony in Compliance with the ALJ's Procedural Schedule") p. 1, section B.1.

SDG&E asserts: "CPA will determine the dollar amount to be provided to [DWR] out of the net revenues received from SDG&E's retail rates." SDG&E February 23, 2001 Proposal for an Interim CPA (entitled preliminary statement) at section labeled "A. Purpose."

[9] In fact, once the CPA is set, its is the Fixed DWR Set Aside that is used to allocate the portion of the CPA that flows to DWR. We do not address the FDWRSA at this time.

[10] As Aglet points out, Water Code Section 80002 states that "Nothing in this division shall be construed to reduce or modify any electrical corporation's obligation to serve."

stabilized their financial condition, and transferred a large amount of their financial risk to DWR. In determining the amount of revenues that DWR should collect, we are also guided by the following relevant statutes adopted by the legislature in AB 1X at the same time it adopted Section 360.5.

Water Code Section 80002.5 states that "[i]t is the intent of the Legislature that power acquired under this division shall be sold to all retail end use customers served by electrical corporations, ..." Water Code Section 80104 explains that "[u]pon the delivery of power to them, the retail end use customers shall be deemed to have purchased that power from the department. Payment for any sale shall be a direct obligation of the retail end use customer to the department." (Emphasis added.) Water Code Section 80106(a) provides a mechanism for DWR to collect payment by providing DWR discretion to contract with utilities to "provide billing, collection, and other related services, as agent of the department, ..." (Emphasis added.) Water Code Section 80110 makes clear that DWR "shall retain title to all power sold by it to retail end use customers." Finally, Water Code Section 80112 explicitly summarizes DWR's interest by stating:

> "... all money paid directly or indirectly to or for the account of [DWR] with respect to any sale ... of power acquired [by DWR] shall constitute property of [DWR] and shall be deposited in the [DWR Electric Power] fund ... To the extent any moneys are received by an electrical corporation pursuant to Section 80106 in the process of collection, and pending their transfer to [DWR], they shall be segregated by the electrical corporation on the terms and conditions established by [DWR] and shall be held in trust for the benefit of [DWR]." (Emphasis added.)

Although Water Code Section 80112 is wholly self-executing, given the positions taken by the utilities in this proceeding, we shall order them to

immediately comply with Water Code Section 80112.[11] Specifically, SDG&E, Edison and PG&E, must immediately segregate, and hold in trust[12] for the benefit of DWR all moneys they receive pursuant to Section 80106. Section VI. E of this order will explain this process in detail.

B. Generation-Related Component of the Retail Rate

We are cognizant that each utility's tariffs contain many different rate schedules. This results in different generation-related rate components for different schedules. In this decision, we do not attempt to calculate the generation-related rate component for each tariff schedule of each utility. Instead, for each utility we will adopt a company-wide average generation-related rate component (except that SDG&E will have separate numbers for capped and uncapped customers).

The generation-related rate component of retail sales is derived from the rates in effect as of January 5, 2001. The 1-cent/kWh surcharge for PG&E and Edison, adopted by the Commission in January, was in place on that date and must be included in the calculation of the generation-related component of the retail rates.

For Edison and PG&E (whose rates are still frozen), the generation-related component of retail rates is calculated as follows:

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[11] In addition to the self-executing nature of Water Code Section 80112, we also premise our action on Water Code Section 80002 (Section 80002). Section 80002 states that nothing in the section should be construed to obligate DWR for procurement cost obligations of SDG&E, PG&E and Edison that may have existed prior to the effective date of AB 1X. The interpretations SDG&E, PG&E and Edison proffer create a risk of imposing such liability upon DWR depending on the use of the revenues the utilities propose improperly to shift to themselves. Section 80002 directs the Commission to issue orders necessary to carry out the section.

[12] Pending transfer to DWR, such money must be held in trust.

Total bundled electric rate (which includes one cent per/kWh surcharge and reflects the legislated 10% rate reduction for those customers to whom it is applicable);

Less non-generation-related rates or charges:

Transmission;[13]

Distribution;

Public Purpose Programs;

Nuclear Decommissioning;

Fixed Transition Amount.[14]

The remainder is the generation-related rate component of retail rates.

SDG&E's rate freeze under AB 1890 has ended and it has no 1 cent/kWh surcharge. SDG&E has an "energy" rate ceiling of 6.5 cents/kWh for residential, small commercial, and street lighting customers, pursuant to AB 265. For these "capped" customers, the generation-related rate component is this 6.5 cent/kWh ceiling. The amount that "uncapped" customers pay for generation varies depending on wholesale market prices. Thus, for SDG&E's uncapped customers the generation-related rate component is necessarily based on an estimate of wholesale prices.

We have relied on the utilities' workpapers (see attachments)[15] to determine each utility's company-wide average generation-related rate

[13] For PG&E this includes the charge called "Reliability Services."

[14] This charge is sometimes referred to as the Trust Transfer Amount.

[15] Attachments B, C, D and E contain a spreadsheet summarizing our results, and workpapers provided by Edison, PG&E, and SDG&E. These workpapers were e-mailed to all parties on February 9, 2001, despite Edison's confidential label. In addition certain other confidential data was used in calculations.

component. Based on our review of these workpapers we adopt the following company-wide average generation-related rate components:

7.277 cents/kWh for Edison;

6.471 cents/kWh for PG&E;

6.5 cents/kWh for SDG&E capped customers;

12.539 cents/kWh for SDG&E uncapped customers.

C. Proposal to Make CPA a Set Rate Component

We propose that the CPA be a set rate component, calculated using utility rate components, as opposed to a periodically changing revenue amount as advocated by the utilities.

Our interpretation that CPA is a "rate" is consistent with language in Section 360.5 which states:

> "The commission shall determine that portion of each existing electrical corporation's retail rate effective on January 5, 2001, that is equal to the difference between the generation related component of the retail rate and the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services. That portion of the retail rate shall be known as the California Procurement Adjustment. ...." (Emphasis added.)

Our interpretation that CPA is "set" and a "rate" is also consistent with Water Code Section 80130 which determines the amount of indebtedness that DWR may incur.

> "... In no event shall [DWR] authorize the issuance of bonds ... in an aggregate amount greater than the amount calculated by multiplying by a factor of four the annual revenues generated by the California Procurement Adjustment ..." (Emphasis added.)

The issuance of bonds is dependent on the CPA. If CPA fluctuated monthly, little certainty would exist concerning the amount of bonds that DWR could issue.[16] An interpretation of Section 360.5 that concludes that the CPA is a set rate is more consistent with Water Code Section 80130. Thus, we reject the utilities' proposals that CPA is an amount that fluctuates monthly. Those proposals focus more on the role of the CPA as a factor in determining the fixed DWR Set-Aside.

The use of the verb "generated" in Water Code Section 80130 also supports our interpretation that CPA is a rate. Amounts do not "generate" revenues, whereas a "rate" would generate revenues.

D. Proposed Method to Calculate the CPA

Under AB 1X, the CPA serves two purposes. It is used as a step in calculating Fixed DWR Set-Aside. In addition, CPA-generated revenues are used to calculate the maximum amount of bonds that DWR may issue. We are not calculating the Fixed DWR Set-Aside at this time.[17]

The following discussion is not adopted by the Commission today. Rather, it incorporates a proposal for the calculation of the CPA, on which we will obtain a further comment from the parties, before being adopted in a subsequent order. The primary purpose for which our proposal to calculate the CPA is made is to enable DWR to proceed with the process of issuing bonds in a timely fashion.

Each of the utilities proposes to calculate the CPA using essentially the following model:

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[16] Some of the utilities' proposals conclude that CPA may sometimes be a negative number. Determining CPA in a manner that yields a negative number is also inconsistent with Water Code Section 80130.

[17] DWR has not asked us to calculate the DWRFSA at this time, and it would be desirable to have more information before we do so.

1. The generation-related component of retail rates is multiplied by the company's total annual kWh sales to produce total generation-related revenues.

2. The four statutorily authorized costs are then subtracted from the revenues calculated above.

As explained elsewhere, we propose to calculate the CPA as a set rate. However, because the statute requires costs to be deducted from rates, this proposal agrees with the utilities that it is appropriate to multiply the generation-related rate-component by total kWh sales[18] to arrive at generation-related revenues. It is then possible to deduct generation-related costs from these revenues. The result of this calculation, however, is not the CPA (which is a rate), but rather it is the revenue produced by the CPA over a given time period (namely the time period over which the kWhs were delivered to customers). We then propose to take these CPA-generated revenues and then divide them by the company's total kWh sales in the same time period to calculate the CPA rate.

After calculating the revenues produced by the generation-related rate component, therefore, this proposal next determines the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services. Section 360.5 expressly refers to those identifiable costs, and no others. Thus, we propose that the only costs to be utilized in calculating the CPA are those specifically enumerated in Section 360.5.

At the workshops, the utilities presented estimates of generation-related costs and of kWh sales, which they used to develop CPA revenues under several different scenarios. Their workpapers and proposals show a number of

[18] For the purpose of this porposed calculation of the CPA, we use total sales to refer to sales by the company and DWR to the utility's bundled service customers, which excludes sales to direct access customers.

adjustments to the total generation-related revenues, as well as a number of categories of costs they believe fall within the four statutorily authorized categories.[19] This proposal does not agree with the utilities that all of these adjustments and costs are appropriate. Section 360.5 clearly refers to those specific identifiable costs. Thus, we propose to exclude from the utilities' submission those costs not specifically provided for in Section 360.5.

For example, we agree with Aglet that franchise fees attach to all retail revenues, not generation costs, and that, uncollectibles are not costs at all, but instead are revenue requirement allowances related to nonpayment of customer bills. Aglet correctly contends that these items are not included in the four categories in Section 360.5. Aglet also correctly argues that while other items such as direct access credits, restructuring implementation costs, employee-related transition costs, losses on sale and QF shareholder incentives conceptually are generation-related costs, they are not encompassed by any of the four categories in Section 360.5. Indeed, since direct access customers are sold electricity by neither the utility nor DWR, direct access revenues and credits both should be excluded from these calculations.[20] We also agree with Aglet that rate reduction bond revenues are not included in any of the four items in Section 360.5. Nuclear incentive amounts--for example, Diablo Canyon ICIP payments--in excess of actual costs are not strictly generation costs but are settled revenue requirement amounts, however, they have not been excluded in our current calculations because we lack the data to do so. Customer Service and

[19] The utilities' workshop workpapers were submitted to the service list in A.00-11-038 et al. on February 9, 2001.

[20] The attached workpapers from SDG&E properly exclude these direct access figures. The scenarios originally submitted by Edison and PG&E included direct access sales in their total sales figures. The Commission has relied on other work papers from these utilities to make the necessary corrections.

Informational expenses and administrative and general (A&G) costs are not generation costs and do not fall within the scope of the four items in Section 360.5.

In order to calculate the CPA we propose to look to the scenarios the utilities provided at the workshops. For Edison and PG&E we propose to use their scenarios which reflect QFs priced at $80/MWh. This figure reflects ongoing efforts to restructure QF pricing. SDG&E provided only one scenario in which it forecasted QF payments in 2001 according to actual contract terms. We propose to correct the selected scenarios to eliminate the adjustments and costs we have found inappropriate (as discussed above). Using these corrected spreadsheets, we propose to calculate the annual revenues generated by the CPA. As shown in Table 1, the annual revenues generated by CPA would be: for PG&E $1,619,592,000, for Edison $801,870,000, for SDG&E capped $293, 596, 000, and for SDG&E uncapped, $ 398, 744, 000. The CPA rate itself would then be calculated by dividing the annual CPA revenues by the company's total annual kWh sales for both utility and DWR supplied energy, excluding Direct Access. The figures produce the following proposed company-wide average CPA rates. For PG&E, 2.180 cents per kWh, for Edison, 1.049 cents per kWh, for SDG&E capped, 2.630 per kWh, for SDG&E uncapped, 8.658 cents per kWh. These calculations would enable DWR to determine the maximum amount of bonds it can issue under Water Code Section 80130.

In using these selected scenarios to calculate the CPA, we would not accepting the utilities' cost figures as a basis for calculating future rates or revenue requirements for the utilities. These cost figures have not been subject to the kind of analysis and scrutiny by the Commission and the parties that would be necessary before we could accept them for such purposes. We would accept them here solely for purposes of calculating the CPA, which we propose to do

primarily in order to permit DWR to determine the maximum amount of bonds it may issue.

E. Segregation of DWR Revenues

Pursuant to Water Code Section 80112:

> "... all money paid directly or indirectly to or for the account of [DWR] with respect to any sale ... of power acquired [by DWR] shall constitute property of [DWR] and shall be deposited in the [DWR Electric Power] fund ... To the extent any moneys are received by an electrical corporation pursuant to Section 80106 in the process of collection, and pending their transfer to [DWR], they shall be segregated by the electrical corporation on the terms and conditions established by [DWR] and shall be held in trust for the benefit of [DWR]." (Emphasis added.)

We have previously ordered the utilities to take these steps with regard to the monies they collect pursuant to Water Code Section 200. The utilities have apparently not done so. According to the utilities, they are uncertain about how to do the necessary calculations. No matter what the stated reason, utilities are holding money that properly belongs to DWR. Elsewhere in this order, we give PG&E and Edison specific directions on how to comply with our prior order. We put them on notice that we will impose penalties if they do not comply promptly.

This leaves us with the issue of how the utilities shall segregate and transfer to DWR the revenues identified in today's order. DWR is purchasing electricity and selling it to retail end-use customers, and it is unreasonable to allow utilities to retain the revenue generated by those transactions — transactions to which they are not a party — even though they are in financial distress. We will shortly outline a methodology which the utilities will be able to use after filing the appropriate tariffs and making any necessary adjustments to their billing systems. However, we will not allow the utilities to retain DWR's

revenues while these details are worked out. Accordingly, this order specifies a method for segregating and transferring revenues to DWR to be used beginning today, until those details are worked out.

DWR reports to each utility on a daily basis the number of kilowatt-hours procured for that utility's end use customers on a given day. Under today's order, DWR is entitled to receive the company-wide average generation-related rate component for each kilowatt-hour that DWR supplies to the utility's retail end-use customers.[21] On average, the utility should receive revenues for the energy supplied by DWR within 45 days after the energy is delivered to retail end use customers.[22] Accordingly, under our immediate methodology, we order the utilities to segregate and hold in trust for DWR, no later than 45 days after DWR supplies power to their retail end-use customers, an amount equal to the product of (i) the number of kilowatt-hours that DWR provided 45-days earlier; and (ii) the company-wide average generation-related rate. Utilities shall segregate these funds according to the method described below. For all electricity supplied by DWR more than 45 days prior to the effective date of today's order, SDG&E, Edison and PG&E shall immediately segregate and hold in trust the funds owing to DWR, except as may otherwise be provided in Section VII of this decision (dealing with funds to be transferred to DWR pursuant to Water Code section 200 and D.01-01-061).

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[21] Elsewhere in this decision we have calculated the company-wide average generation-related rate for each utility. Until such time as schedule specific generation-related rates are calculated, the utilities will use the company-wide average generation-related rate for determining the sums they must transfer to DWR.

[22] The utilities typically use a 30-day billing period. Thus, on average, there is approximately 15 days from the date the electric service is provided until the bill is rendered. Utility bills are generally due less than 30 days after being rendered. Thus, on average, the utilities should receive revenues for the power supplied by DWR within 45 days after the power is delivered to retail end use customers.

Because SDG&E has two separate average generation-related rates (one for capped customers and one for uncapped customers), this immediate methodology must be modified for SDG&E. Because SDG&E has two separate average generation-related rates, SDG&E must divide the "kilowatt hours that DWR provided 45-days earlier" between capped and uncapped customers. Pursuant to Water Code section 80002.5 "[p]ower sold by the department to retail end use customers shall be allocated pro rata among all classes of customers to the extent practicable." Accordingly, the total kilowatt hours supplied by DWR should be attributed to capped and uncapped customers based on the ratio of total kilowatt hours delivered by SDG&E to capped and uncapped customers. This information will have to come from SDG&E's billings; however, SDG&E's bills cover a period of approximately 30-days, not a single day. The billing information SDG&E uses to implement this immediate methodology should cover a period as close in time as possible to the date on which the DWR power was sold to SDG&E's end use customers. This information may cover billings rendered on a single day, or over a period of a month. However, SDG&E must use a consistent method for calculating the percentage of power attributed to capped and uncapped customers throughout the period covered by this immediate methodology. Using a methodology substantially along the foregoing lines, SDG&E should divide the kilowatt-hours supplied by DWR 45 days earlier between capped and uncapped customers. Then the kilowatt-hours for each type of customers should be multiplied by the corresponding company-wide average generation related rate, to produce a dollar amount. SDG&E should then segregate, for the benefit of DWR, the sum of the dollar amounts for capped and uncapped customers.

A more precise method for remitting funds to DWR should be arrived at as soon as practicable. Under this more precise methodology, each customer's

bill will specifically identify the generation-related rate for DWR. In order to do this, tariff schedule-specific generation-related rates will need to be calculated. In addition, it will be necessary to determine the number of DWR supplied kilowatt-hours on each customer's bill to which this customer specific generation-related rate will be applied. The number of DWR-supplied kilowatt-hours will be calculated using the following method.

First, each utility will calculate the percentage of DWR power supplied to its customers for each day, by dividing (1) the amount of power supplied by DWR and distributed by the utility by (2) the sum of (a) the amount of power generated or purchased by the utility, including any real time energy from the Independent System Operator, and (b) the amount of power included in (1) above.[23]

Because each customer's billing cycle includes more than one day, the utility will calculate the percentage of DWR power over a billing cycle by averaging the percentage of DWR power supplied for each day in the customer's billing cycle (the DWR billing-cycle percentage). Finally, the utilities will calculate the amounts they must collect on behalf of DWR as required by today's order by multiplying the total kilowatt-hours on a customer's bill by the DWR billing-cycle percentage and then multiplying that product by the schedule specific generation-related rate. This will show the amount on each customer's bill that is required to be collected by the utility on behalf of DWR, and once collected immediately segregated and held in trust for the benefit of DWR until it is transmitted to DWR, all as more specifically described below.

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[23] For example, if on a given day a particular utility generates or purchases (from QFs and others) 750 megawatt hours of power and distributes to its customers a further 250 megawatt hours of DWR power for a total of 1,000 MWh, the percentage of DWR power supplied for that day would be 25%.

Within 15 days of today's order, each utility shall file the tariff changes necessary to implement this more precise methodology, and shall implement billing under this more precise methodology within 30 days of the approval, by the Commission or its staff, of these tariff changes.

At various places in this order, we have referred to the segregation of funds that are to be paid to DWR. Such funds are to be collected by the utility as agent for DWR, and segregated and held in trust for DWR in a separate bank account (denominated, "[utility name] in trust for the Department of Water Resources") for the benefit of DWR until such time as those funds shall be paid over to DWR in accordance with this order. Unless doing so would contravene an existing agreement or require the use of a bank outside California, such accounts shall be opened with a bank that has not extended credit or made credit available to the utility. The utility shall not have any right in and to such revenues and such revenues shall not be used by the utility as its own or commingled with its own monies. At all times such revenue shall constitute property of DWR only, as provided by statute.

We are concerned that our past orders with regard to the segregation of funds have not been carried out, and direct the utilities to provide, by letter to the Commission's Executive Director, and to the Director of the Department of Water Resources, the numbers of these accounts, the names of the banks where the accounts are located, the amount of credit that has been extended or made available to the utility by that bank, and the amounts deposited therein. Such letter shall be delivered by fax no later than 4:00 p.m. on March 28, 2001.

Moreover, utilities should transfer all funds held in trust accounts for DWR, including all interest paid thereon, each business day, before 10:00 am, Pacific Time. Each minute of delay in complying with this order shall constitute a separate violation of this order. We find that the above payment mechanisms

are essential and necessary to accomplish the directives of Water Code Section 80112.

VII. D.01-01-061

In D.01-01-061, we ordered Edison and PG&E to collect, in trust for the benefit of DWR, sums owed by retail end-use customers. Further, we directed Edison and PG&E to make monthly payments to DWR. To date, it appears that Edison and PG&E have not made any payment to DWR pursuant to Ordering Paragraph 7 of D.01-01-061. We will order Edison and PG&E to pay DWR, in a lump sum, by 9:00 a.m. on the day following the effective date of this decision the amounts due under Ordering Paragraph 7 of D.01-01-061. In the event Edison and PG&E believe they are unable to calculate the amounts owed to DWR, they shall calculate the amounts owed to DWR as follows. Each utility shall pay DWR for the number of kWhs that DWR asserts it provided to that utility's retail end-use customers pursuant to Water Code section 200. Edison shall pay a rate of 6.277 cents for each such kWh. PG&E shall pay a rate of 5.471 cents for each such kWh.[24] If the payment is not made when required, the Commission will assess penalties against the utility for each day that payment is late, pursuant to Chapter 11 of the Public Utilities Act. The officers and employees of the utility are also subject to sanctions under Chapter 11.

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[24] These amounts were derived from the company-wide average generation-related rates adopted above. D.01-01-061 ordered the "net amount charged for electric energy" to be transferred to DWR for the kWhs DWR supplied to Edison's and PG&E's end-use customers. This net amount is essentially the same as the generation-related rates adopted above, except that it did not include the 1-cent/kWh surcharge. Accordingly, we have reduced the adopted company-wide average generation-related rates by 1-cent/kWh to determine the amount per kWh to be transferred to DWR pursuant to D.01-01-061. We remind Edison and PG&E that D.01-01-061 covered only the electricity supplied pursuant to Water Code section 200. Thus, all other amounts to be transferred to DWR pursuant to today's decision include the 1-cent/kWh surcharge.

VIII. Proposal to Issue Financing Order

DWR requests that we determine the CPA for each utility as part of an order, and that we acknowledge that the Department may rely upon this determination for purposes of Section 80130 of the Water Code. DWR further proposes that upon its written acceptance thereof, our order would constitute an agreement between DWR and the Commission within the meaning of Water Code Section 80110. That statute provides in relevant part that:

"The commission may enter into an agreement with the department with respect to charges under Section 451 for purposes of this division, and that agreement shall have the force and effect of a financing order adopted in accordance with Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the Public Utilities Code, as determined by the commission."

This provision must be read in conjunction with Water Code Section 80130, which provides in relevant part that:

"In addition, before the issuance of bonds, the department shall establish a mechanism to ensure that the bonds will be sold at investment grade ratings and repaid on a timely basis from pledged revenues. This mechanism may include, but is not limited to, an agreement between the department and the commission as described in Section 80110."

The Legislature clearly anticipated that the Commission and DWR would enter into necessary agreements to ensure the marketability of the bonds. Determination of both the CPA and the annual revenues produced by the CPA are key steps in determining the maximum amount of bonds that may be issued. DWR should be able to rely upon these determinations. Accordingly, with respect to our determination of the CPA rate and the annual revenues generated

by the CPA, we propose to accept DWR's request. Upon their written acceptance by the department, the determinations of both the CPA and the annual revenues produced by the CPA made herein would constitute a rate agreement between DWR and the Commission within the meaning of Section 80110 of the Water Code, and such agreement would have the full force and effect of a financing order.

IX. Motions to Strike TURN's Comments

The motions of Edison, PG&E and SDG&E to strike the comments of TURN are denied. We value the comments of all participants in our proceedings.

X. Comments on Decision

Under Pub. Util. Code Section 311(g)(3) and Rule 77.7(f)(9) of the Rules of Practice and Procedure, the Commission may determine on its own motion that public necessity requires reduction or waiver of the 30-day public review and comment period set by Pub. Util. Code Section 311(g)(1). We have weighed the interest in allowing the full comment period against the need for DWR to begin to receive revenue collected by the utilities for electricity DWR has sold to customers, and against the need to provide DWR with certainty about the revenues that will be generated by the CPAs of the three utilities. We conclude that the public interest in providing certainty at an early date, especially in the current energy crisis, outweighs the interest in allowing a full comment period. Therefore, this period is waived on all of this decision except for sections VI C and D, and section VIII, and the corresponding proposed findings of fact and conclusions of law. The comment period on sections VI C and D, and section VIII, and the corresponding proposed findings of fact and conclusions of law will reduced with comments due at 5:00 p.m. on Thursday, March 30, 2001.

XI. Proposed Findings

1. CPA is a set rate.

2. A utility's CPA is calculated by dividing CPA-generated revenues by the company's total kWh sales.

3. Franchise fees, uncollectibles, direct access credits, restructuring implementation costs, employee-related transition costs, losses on sale and QF shareholder incentives, rate reduction bond revenues, nuclear incentive amounts, customer service and informational expenses and administrative and general (A&G) costs should be excluded from utility costs for the purpose of calculating the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services pursuant to Pub. Util. Code Section 360.5.

4. The cost figures the utilities included in their workpapers are useful for the sole purpose of calculating CPA to permit DWR to determine the maximum amount of bonds it may issue.

5. Determination of both the CPA and the annual revenues produced by the CPA are key steps in determining the maximum amount of bonds that may be issued.

XII. Proposed Conclusions of Law

1. In using selected scenarios from the utilities' work papers to calculate the CPA, we are not accepting the utilities' cost figures as a basis for calculating future rates or revenue requirements for the utilities; we accept them here solely for purposes of calculating the CPA, which we do today primarily in order to permit DWR to determine the maximum amount of bonds it may issue.

2. The determination of the CPA rate and the annual revenues generated by the CPA should, upon acceptance in writing by the California Department of Water Resources (DWR), constitute an agreement between this Commission and DWR within the meaning of Water Code Section 80110, and as such should have the full force and effect of a financing order adopted in accordance with Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the Public Utilities Code.

XIII. Findings of Fact

1. When retail end-use customers being served by utilities take delivery of power procured by DWR, the retail end-use customers are deemed to have purchased the power from DWR..
2. DWR power is to be allocated pro rata among all classes of retail end-use customers to the extent possible.
3. The California Department of Water Resources (DWR) set forth in a letter to the Commission dated March 14, 2001, its views on how the Commission should determine the CPA..
4. Establishing the CPA is important to any long-term or short-term financing.
5. DWR's power purchases and sales to retail end-use customers relieve utilities of the costs for the net short procured by DWR..
6. For the sale of net short energy to the customers of each utility, DWR should receive a per-kWh price equal to the applicable generation-related retail rate per kilowatt-hour established for each utility as in effect on January 5, 2001. This is not the sole source of revenue to which DWR may be entitled.

7. The Fixed DWR Set-Aside is portion of the utility's CPA that the Commission allocates to the DWR..
8. Calculation of the CPA does not alter DWR's right to recover any portion of its revenue requirement which is not fully recovered through existing rates.
9. Upon the delivery of DWR power to retail end use customers, such customers are deemed to have purchased that power from DWR..
10. Payment for any sale of DWR power is a direct obligation of the retail end use customer to DWR..
11. DWR's procurement of power improves the financial stability of SDG&E, PG&E and Edison.
12. The generation related rate component (and in turn the CPA) is derived from rates in effect as of January 5, 2001.
13. The generation related rate component (and in turn the CPA rate) includes the 1-cent/kWh surcharge adopted by D.01-01-018.
14. For Edison and PG&E the generation-related component of retail rates should be equal to the total bundled electric rate (including 1 cent/kWh surcharge and reflecting the legislated 10% surcharge for those customers to whom it is applicable) less the following non-generation-related rates or charges:

    Transmission (including "reliability services" for PG&E)

    Distribution

    Public Purpose Programs

    Nuclear Decommissioning

    Fixed Transition Amount.

15. For customers subject to SDG&E's rate ceiling of 6.5¢/kWh, the generation-related rate component is 6.5 cent/kWh.

16. For customers not subject to SDG&E's rate ceiling, the generation-related rate component is based on an estimate of wholesale prices.
17. Each utility's tariffs contain many different rate schedules resulting in different generation-related rate components for different schedules.
18. The company-wide average generation-related rate component for Edison is 7.277 ¢/kWh.
19. The company-wide average generation-related rate component for PG&E is 6.471¢/kWh.
20. The company-wide average generation-related rate component for SDG&E capped customers is 6.5 ¢/kWh.
21. The company-wide average generation-related rate component for SDG&E uncapped customers is 12.539 ¢/kWh.
22. Under AB 1X, the CPA serves as a step in calculating the Fixed DWR Set-Aside and also the maximum amount of bonds that DWR may issue.
23. PG&E and Edison apparently have not complied with the requirement in D.01-01-061 to segregate and transfer to DWR, consistent with D.01-01-061, the revenues received for charges paid by retail end use customers for energy sold by DWR. pursuant to Water Code section 200.
24. For all power not covered by D.01-01-061, until such time as billing begins under schedule-specific generation-related rates, DWR is entitled to receive the company-wide average generation-related rate component for each kilowatt-hour that DWR supplies to the utility's retail end use customers.
25. Unlike Edison and PG&E, which each have only one average generation-related rate, SDG&E has two separate average generation-related rates, one for capped and one for uncapped customers.

26. With respect to SDG&E, to give effect to the requirement of Water Code Section 80002.5 that "[p]ower sold by the department to retail end-use customers shall be allocated pro rata among all classes of customers to the extent practicable," it is necessary to modify the immediate methodology for segregating and transferring revenues to DWR that we adopt for Edison and PG&E.

27. We have weighed the interest in allowing the full comment period against the need for DWR to begin to receive revenue collected by the utilities for electricity DWR has sold to customers, and against the need to provide DWR with certainty about the revenues that will be generated by the CPAs of the three utilities and concluded that the public interest in providing certainty at an early date outweighs the interest in allowing a full comment period.

XIV. Conclusions of Law

1. DWR should receive payment for power it purchases and sells to retail end-use customers.
2. DWR is entitled to an amount equal to the number of kWh sold to retail end-use customers multiplied by the relevant generation-related rate.
3. Monies other than the CPA may flow to DWR.
4. DWR retains title to all power sold by it to retail end use customers.
5. Utilities must deposit, in the DWR Electric Power Fund, all money paid directly or indirectly to or for the account of DWR with respect to any sale of power acquired by DWR.
6. All money paid directly or indirectly to or for the account of DWR with respect to any sale of power acquired by DWR shall constitute property of DWR.

7. Utilities, on terms and conditions established by DWR, must segregate any moneys received in the process of collection, and pending their transfer to DWR by the utility, must hold such monies in trust for the benefit of DWR.
8. It is unreasonable for utilities to retain the revenue generated from DWR purchases of electricity that is sold to the utilities' retail end use customers, even though they are in financial distress. Except as otherwise required by Ordering Paragraph 8, until such time as schedule specific generation-related rates are calculated, the utilities should use the company-wide average generation-related rate for determining the sums they must transfer to DWR.
9. Except as otherwise required by Ordering Paragraph 8, until such time as schedule specific generation-related rates are calculated: No later than forty-five days after DWR supplies power to the utilities' retail end use customers the utility should remit to DWR an amount equal to the product of the number of kilowatt-hours that DWR provided 45-days earlier and the company-wide generation-related rate.

10. For SDG&E, the immediate methodology for segregating and transferring revenues to DWR should reflect the fact that SDG&E has two separate average generation-related rates, one for capped and one for uncapped customers.
11. Except as otherwise required by Ordering Paragraph 8, for all electricity supplied by DWR more than 45-days prior to the effective date of today's order the utility shall immediately segregate and hold in trust the funds owing to DWR.
12. SDG&E, Edison and PG&E should submit tariff schedule-specific generation-related rates so that each customer's bill will specifically

identify the generation-related rate for DWR and the amount the utility is collecting on behalf of DWR.

13. SDG&E, Edison and PG&E should determine the number of DWR supplied kilowatt-hours on each customer's bill to which this customer specific generation-related rate will be applied using the method set forth in this decision.

14. The utility shall not have any right in and to DWR revenues and such revenues shall not be used by the utility as its own or commingled with its own monies. At all times such revenue shall constitute property of DWR only.

15. The payment mechanisms established in this decision are essential and necessary to accomplish the directives of Water Code Section 80112.

16. Edison and PG&E should comply with Ordering Paragraph 7 of D.01-01-061 by 9:00 a.m. on the day following the effective date of this decision. If Edison and PG&E are unable to calculate the amounts owed to DWR pursuant to D.01-01-061, each utility shall pay DWR for the number of kWhs that DWR asserts it provided to that utility's retail end-use customers pursuant to Water Code section 200. Edison shall pay a rate of 6.277 cents for each such kWh. PG&E shall pay a rate of 5.471 cents for each such kWh.

17. The motions of Edison, PG&E and SDG&E to strike the comments of TURN should be denied.

18. Pursuant to Pub. Util. Code Section 311(g)(3) and Rule 77.7(f)(9) of the Rules of Practice and Procedure, waiver of comments on the draft decision is necessary in the public interest, except that there should by a reduced comment period on sections VI.C. and VI.D and section VIII. of

this decision and the corresponding proposed findings of fact and conclusions of law.

INTERIM ORDER

IT IS ORDERED that:

1. The company-wide average generation related rates are 7.277 cents per kWh for Edison, 6.471 cents per kWh for PG&E, 6.5 cents per kWh for SDG&E capped customers, and 12.539 cents per kWh for SDG&E uncapped customers.

2. Until such time as billing begins under schedule specific generation-related rates, the San Diego Gas & Electric Company (SDG&E), Southern California Edison Company (Edison) and Pacific Gas and Electric Company (PG&E) must use the company-wide average generation-related rates established in Ordering Paragraph 1 of this decision for determining the sums they must transfer to DWR pursuant to Ordering Paragraphs 3 and 4 except as otherwise provided by Ordering Paragraph 8.

3. SDG&E, Edison and PG&E shall segregate and hold in trust for DWR, no later than forty-five days after DWR supplies power to their retail end use customers an amount equal to the product of the number of kilowatt-hours that DWR provided 45 days earlier and the company-wide average generation-related rate. For SDG&E, the total kilowatt hours supplied by DWR shall be attributed to capped and uncapped customers based on the ratio of total kilowatt hours delivered by SDG&E to capped and uncapped customers. SDG&E shall use a consistent method, based on its billings, in accordance with the discussion section of this decision, for calculating the percentage of power attributed to capped and uncapped customers throughout the period covered by this immediate methodology for segregating and transferring sums to DWR.

4. For all electricity supplied by DWR more than 45 days prior to the effective date of today's order, SDG&E, Edison and PG&E shall immediately segregate and hold in trust the funds owing to DWR, except as otherwise provided in Ordering Paragraph 8.

5. Within 15 days of today's order, each utility shall file the tariff changes necessary to implement the more precise billing methodology set forth in this decision and shall implement billing under this more precise methodology within 30 days of the approval, by the Commission or its staff, of the tariff changes.

6. In all cases funds and revenues that are to be paid to DWR shall be collected by the utility as agent for DWR, and segregated and held in trust for DWR in a separate bank account (denominated, "[utility name] in trust for the Department of Water Resources") for the benefit of DWR until such time as those funds shall be paid over to DWR in accordance with this order. Unless doing so would contravene an existing agreement or require the use of a bank outside California, such accounts shall be opened with a bank that has not extended credit or made credit available to the utility. The utility shall not have any right in and to such funds and revenues, and such funds and revenues shall not be used by the utility as its own or commingled with its own monies. At all times such funds and revenues shall constitute property of DWR only, as provided by statute. Edison, PG&E, and SDG&E shall each transfer all funds held in trust accounts for DWR, including all interest paid thereon, each business day before 10:00 a.m., Pacific Time.

7. Edison, PG&E, and SDG&E shall each provide, by letter to the Commission's Executive Director and to the Director of the Department of Water Resources, the numbers of these bank accounts, the names of the banks where the accounts are located, the amount of credit that has been extended or made

available to the utility by the bank, and the amounts deposited therein. Such letter shall be delivered by fax no later than 4:00 p.m. on March 28, 2001.

8. Edison and PG&E shall pay DWR by 9:00 a.m. on the day following the effective date of this decision the sums owed pursuant to Ordering Paragraph 7 of D.01-01-061. If Edison and PG&E are unable to calculate the amounts owed to DWR pursuant to D.01-01-061, each utility shall pay DWR for the number of kWhs that DWR asserts it provided to that utility's retail end-use customers pursuant to Water Code section 200. Edison shall pay a rate of 6.277 cents for each such kWh. PG&E shall pay a rate of 5.471 cents for each such kWh.

9. The motions of Edison, PG&E and SDG&E to strike the comments of TURN are denied.

10. Comments on sections VI.C and D and section VIII of this decision and the corresponding proposed findings of fact and proposed conclusions of law shall be filed and served no later than 5:00 p.m. on Thursday, March 29, 2001. Each utility shall include in its comments a revised version of that portion of the Spreadsheet included as Attachment E to this Decision that relates to that utility. This revised spreadsheet shall exclude in its calculation of Utility Related Costs those nuclear incentive amounts (e.g., Diablo Canyon ICIP payments) in excess of actual costs, and be accompanied by appropriate supporting work papers. Any party asserting that the figures contained in Attachment E contain miscalculations should submit a revised version of Attachment E correcting the alleged errors, which should be accompanied by appropriate work papers.

This order is effective today.

Dated March 27, 2001, at San Francisco, California.

LORETTA M. LYNCH
President
HENRY M. DUQUE
RICHARD A. BILAS
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners

I will file a concurring opinion.

/s/ RICHARD A. BILAS
Commissioner

ATTACHMENT A

DEPARTMENT OF WATER RESOURCES (Letterhead)

March 14, 2001

Commissioners Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102

Dear Commissioners:

This letter is submitted by the Department of Water Resources (the "Department") for your consideration in connection with the determination by the Commission of the "California Procurement Adjustment" mentioned below. The Department respectfully requests that the Commission determine the California Procurement Adjustment consistent with what the Department believes to be the clear meaning of Assembly Bill No. 1 from the First Extraordinary Session ("ABX1-1"), Chapter 4, Statutes of 2001, as described below.

Governor Davis signed ABX1-1 on January 31, 2001. Section 2 of ABX1-1 adds Section 360.5 to the Public Utilities Code, which reads as follows:

> 360.5 The commission shall determine that portion of each electrical corporation's retail rate effective on January 5, 2001, that is equal to the difference between the generation related component of the retail rate and the sum of the costs of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services. That portion of the retail rate shall be known as the California Procurement Adjustment. The commission shall further determine the amount of the California Procurement Adjustment that is allocable to the power sold by the [D]epartment. That amount shall be payable, by each electrical corporation, upon receipt by the electrical corporation of the revenues from its retail end use customers, to the [D]epartment for deposit in the Department of Water Resources Electric Power Fund, established by Section 80200 of the Water Code. The amount determined pursuant to this

subdivision shall be known as the Fixed Department of Water Resources Set-Aside.

For compelling and practical reasons, the Commission's determination of the California Procurement Adjustment (the "CPA") is a critical element in the implementation of ABX1-1. It is the initial step in establishing an important revenue source for the Department in meeting its power purchase responsibilities. It is also important to any long-term or short-term financing by the Department.

In their filings in this proceeding, the electrical corporations make the unwarranted assertion that, in enacting ABX1-1, the Legislature not only afforded relief to the utilities with respect to procurement of the so-called "net short," but that the Legislature also granted them, in effect, a rate increase on the portion of the power which they continue to supply. The clear meaning of ABX1-1 is very different. Section 360.5 was intended to address important changes in circumstances that arose from the enactment of ABX1-1. Through the enactment of Section 360.5, the Legislature recognized that a significant portion of the electrical corporation's costs intended to be recovered in established generation rates were no longer being borne by the electrical corporations to the extent that the Department purchased the "net short" and that an appropriate adjustment in generation rates was therefore required. Section 360.5 was also clearly intended to provide financial assurance to the Department for its power purchases pursuant to ABX1-1 by making available to the Department (to the extent of the Commission-determined "Fixed Department of Water Resources Set-Aside") the portion of the rate applicable to each corporation that was intended to be applied by the corporation to pay for the "net short" being purchased by the Department.

In order to address these changes in circumstances, ABX1-1 envisions that for the Department's sale of "net short" energy to the customers of each electrical corporation, the Department will initially receive (i) a per-kWh price equal to the applicable generation-related retail rate per kilowatt-hour established for each electrical corporation as in effect on January 5, 2001 plus (ii) a Commission-determined portion of the January 5, 2001 rate for power the electrical corporation continues to sell. Consequently, ABX1-1 provides that each electrical corporation will continue to receive—on a per-kWh basis—only (i) the components of the January 5, 2001 rate attributed at the time of original rate-making to power that the corporation will continue to sell to its retail end use customers, (*i.e.*, native generation, qualifying facility contracts, existing bilateral

contracts and ancillary services) plus (ii) a Commission-determined portion of the January 5, 2001 rate for power the electrical corporation continues to sell, (*i.e.*, the portion of such rate which is not determined to be part of the Fixed Department of Water Resources Set-Aside. Nothing in ABX1-1 suggests that the electrical corporations are to retain any revenues attributable to power furnished by the Department and to allow them to do so was certainly not the intent of ABX1-1.

As Section 360.5 states, the CPA is a portion of a "retail rate effective on January 5, 2001." Therefore the CPA itself is a rate, to be expressed in terms of cents per kilowatt-hour (as Section 80130 of the Water Code also requires, as discussed below). Section 360.5 calls for the following determinations and calculations with regard to each electrical corporation:

First: Identify the generation related component of the corporation's retail rate that was in effect on January 5, 2001, expressed in terms of cents per kilowatt-hour (the "Total Generation Related Rate").

Second: Determine the "sum of the costs" (also expressed as a rate, *i.e.*, in terms of cents per kilowatt-hour) imputed at the time of rate-making by the Commission in connection with the establishment of the January 5, 2001 rate, to the corporation's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services (the "Utility Retained Rate").

Third: Determine "the difference between" the Total Generation Related Rate and the Utility Retained Rate. That is, subtract the Utility Retained Rate from the Total Generation Related Rate to determine the CPA applicable to the electrical corporation. (Note that, under the language of Section 360.5, since the CPA is "a portion of the Total Generation Related Rate, it cannot be negative.)

Section 360.5 requires that each electrical corporation pay to the Department, upon receipt of payment by each of its end use customers for power sold by the electrical corporation (as opposed to power deemed sold to such user by the Department), all or a portion of an amount equal to the product of (i) the number of such kilowatt-hours purchased by the user from the electrical

corporation, multiplied by (ii) the electrical corporation's CPA. That portion of the CPA to be paid to the Department is the Fixed Department of Water Resources Set-Aside. Please note that the Department is not requesting that the Commission determine the Fixed Department of Water Resources Set-Aside at this time.

Following is an example which illustrates the CPA calculation methodology required by ABX1-1. Assume that (i) a hypothetical utility delivers to its retail end use customers 100 kWh annually, half of which is power derived from the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services, and the other half of which is "net short" power. Further assume that the hypothetical utility's Total Generation Related Rate is 5¢ per kWh, which took into account and consisted of an imputed cost of the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services of 2¢ per kWh at the time the Total Generation Related Rate was determined and the cost of the "net short" power of 8¢ per kWh at the time the Total Generation Related Rate was determined. (The 2¢ per kWh imputed cost of 50 kWh ($1.00) and the 8¢ per kWh imputed cost of the other 50 kWh ($4.00) result in an average blended cost of 5¢ per kWh for all 100 kWh. In other words, the "Total Generation Related Rate" for the hypothetical utility is 5¢ per kWh.) In the example, the difference between the 5¢ per kWh Total Generation Related Rate and the 2¢ imputed cost of the power which the utility will continue to sell from the utility's own generation, qualifying facility contracts, existing bilateral contracts, and ancillary services equals a CPA of 3¢ per kWh. In this example, the CPA of 3¢ per kWh would be subject to further allocation by the Commission to determine the Fixed Department of Water Resources Set-Aside.

Confirmation that the Legislature's intended construction of Section 360.5 is consistent with the CPA calculation methodology described above can be found in Section 80114 of the Water Code, enacted as part of ABX1-1, which provides as follows:

> 80114. The commission shall take those actions necessary to ensure that all, or a portion of, the component rates that are available to electrical corporations for the purchase of their net short position of electricity are used to recover the revenue requirements established pursuant to this division.

Consistent with the language of ABX1-1, since the January 5, 2001 retail rate—and, therefore, the components of the CPA—took into account historical costs, the CPA is fixed and immutable. It is not affected by any change in the costs of any generation resource of any electrical corporation that was not reflected in the January 5, 2001 rate at the time such rate was originally determined. On the other hand, the calculation of the CPA, in and of itself, does not alter the right of the Department to recover any portion of its revenue requirements which is not fully recovered through the application of the portion of the CPA equal to the Fixed Department of Water Resources Set-Aside (nor does it affect any right of the Commission to allow additional cost recovery to the utilities for the portion of the power for which they remain responsible, subject, to applicable law and Commission proceedings). Further, the calculation of the CPA does not quantify the division of the CPA as between the Department and any electrical corporation (*i.e.*, the determination of the Fixed Department of Water Resources Set Aside). The Department requests that Commission effectuate that division through a later determination and requests that the Commission's determination at this time be limited to the determination of the California Procurement Adjustment.

ABX1-1 also enacted Division 27 (commencing with Section 80000) of the Water Code. Division 27 established in the State Treasure the Department of Water Resources Electric Power Fund (the "Fund") and authorized the Department to issue bonds, notes, and other evidences of indebtedness (collectively, "Bonds") for certain limited purposes, including:

- paying the costs of electric power and transmission, scheduling, and other related expenses, or to reimburse expenditures from the Fund for those purposes.

- repaying to the General Fund certain advances made to the Department for the power purchase program; and

- establishing or maintaining reserves in connection with the Bonds and paying certain costs incidental to the issuance, payment and security of the Bonds.

Section 80130 of the Water Code (the "Bond Cap"), enacted as part of ABX1-1, provides in relevant part as follows (emphasis added):

> In no event shall the [D]epartment authorize the issuance of bonds ... in an aggregate amount greater than the amount calculated by multiplying by a factor of four the annual revenues generated by the California Procurement Adjustment, as determined by the [C]ommission pursuant to Section 360.5.

During the Legislature's consideration of ABX1-1, the bill's author communicated to the Legislature his expectation that the amount of the Bond Cap that would result from the application of Section 80130 would approximate $10 billion. Many Legislators cited the $10 billion figure during the floor debate of ABX1-1. The phrase "generated by" – used in Section 80130—is further evidence that the CPA is a rate to be expressed in terms of cents per kilowatt-hour and not a dollar amount of revenues. Consistent with Section 80130 of ABX1-1, the Department will determine the Bond Cap by calculating the dollar amount of the annual revenues which would be generated by the applicable CPA (as determined by the Commission) in each electrical corporation's service area, adding such dollar amounts and multiplying the resulting sum by four.

The Department requests that the Commission (i) determine, as part of an order, the CPA of each electrical corporation pursuant to Section 360.5 and in accordance with the methodology discussed above, and (ii) acknowledge that the Department may rely upon such determination for the purposes of Section 80130 of the Water Code.

In addition, we request that the order provide that, upon its acceptance by the Department in writing, the order will constitute an agreement between the

Department and the Commission within the meaning of Section 80110 of the Water Code and that, pursuant to Section 80110, the order will have the full force and effect of a financing order.

Thank you for your assistance and attention to this important matter. We will be submitting additional information and requests to the Commission relating to the Department's power purchase program and financing plans and appreciate your continuing cooperation.

Sincerely,

/s/ THOMAS M. HANNIGAN

Thomas M. Hannigan
Director

(END OF ATTACHMENT A)

Attachment B

1. QF Payment @ $80/MWh
2. Includes Imputed RRB Credits

Southern California Edison Company
Calculation of California Procurement Adjustment
(As Set Forth In ABX1)
(Unless Denoted Otherwise, Amounts are in Thousands)

Line No.	Component	2001 Estimate February	March	April	May	June	July	August	September	October	November	December	Total
1.	Total Delivered Sales (Metered GWh)	6,290	6,715	6,419	6,722	7,029	7,491	8,275	7,573	7,619	6,663	6,665	77,461
2.	Generation Rate As of 1-05-01 ($/MWh)	56.85	56.85	56.85	56.85	63.46	73.37	73.37	73.37	66.76	56.85	56.85	63.40
3.	Emergency Procurement Surcharge ($/MWh)	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
4.	Generation Rate + EPS ($/MWh)	66.85	66.85	66.85	66.85	73.46	83.37	83.37	83.37	76.76	66.85	66.85	73.40
5.	Gross Generation Revenue	(420,491)	(448,867)	(429,135)	(449,338)	(516,369)	(624,491)	(689,869)	(631,351)	(584,874)	(445,435)	(445,551)	(5,685,772)
Adjustments:													
6.	Franchise Fees and Uncollectibles	4,717	5,035	4,814	5,040	5,792	7,005	7,738	7,082	6,561	4,996	4,998	63,777
7.	Direct Access Credit	39,083	41,720	39,886	41,764	47,994	58,044	64,120	58,681	54,362	41,401	41,412	528,467
8.	RMR	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	36,255
9.	Restructuring Implementation	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	30,805
10.	Other Authorized Costs/Credits	7,236	7,205	7,174	7,143	7,112	7,081	7,050	7,019	6,988	6,957	6,926	77,891
11.	Imputed 10% Rate Reduction	(27,814)	(31,663)	(27,926)	(29,852)	(32,524)	(36,685)	(42,554)	(36,322)	(33,843)	(31,268)	(31,130)	(361,582)
12.	Imputed TTA	(22,637)	(26,571)	(21,369)	(24,313)	(29,005)	(29,254)	(37,448)	(30,544)	(26,960)	(23,893)	(22,897)	(294,891)
13.	**Generation-Related Component**	**(413,809)**	**(447,044)**	**(420,460)**	**(443,458)**	**(510,904)**	**(612,204)**	**(684,866)**	**(619,339)**	**(571,671)**	**(441,145)**	**(440,146)**	**(5,605,048)**
14.	Generation-Related Rate ($/MWh)	72.61	73.49	72.29	72.82	80.22	90.21	91.35	90.27	82.81	73.08	72.89	79.87
Less:													
15.	A. SCE Owned Generation Rev Rqmt:												
16.	Capital Related	24,612	24,612	24,612	24,612	24,612	24,610	24,608	24,608	24,605	24,603	24,605	270,694
17.	SONGS ICIP	32,282	49,393	47,798	49,393	47,798	49,393	49,393	47,798	49,393	47,798	49,393	519,829
18.	Other On-Going (PV, Coal, and Hydro)	32,546	33,210	28,083	32,442	32,818	34,851	35,879	34,629	33,767	35,808	35,996	370,027
19.	Subtotal	89,439	107,214	100,492	106,446	105,228	108,853	109,879	107,035	107,764	108,208	109,993	1,160,551
20.	B. QF Payments:												
21.	QF Energy and Capacity Costs ($80)	174,400	158,240	176,080	171,600	179,440	174,640	178,480	176,560	168,400	174,000	166,800	1,898,640
22.	QF Buyouts	3,587	6,712	20,395	3,587	6,712	20,395	3,587	6,712	20,395	3,587	7,024	102,693
23.	Shareholder Incentives	-	-	-	-	-	-	-	-	-	-	-	-
24.	Scheduling, Dispatch & Admin	70	70	70	70	70	70	70	70	70	70	70	770
25.	Subtotal	178,057	165,022	196,545	175,257	186,222	195,105	182,137	183,342	188,865	177,657	173,894	2,002,103
26.	C. Bilateral Contract Costs:												
27.	Interutility Net Contract Costs	9,836	10,372	10,712	9,239	10,420	11,760	11,775	12,082	12,433	10,352	10,568	119,549
28.	Interutility Buyouts	-	-	-	-	-	-	-	-	-	-	-	-
29.	Scheduling, Dispatch & Admin	262	262	262	262	262	262	262	262	262	262	262	2,877
30.	BFM Contracts Costs	-	-	-	-	-	-	-	-	-	-	-	-
31.	Bilateral Contract Costs	11,752	13,032	12,557	12,984	12,605	17,679	17,775	17,099	15,624	14,957	15,336	161,400
32.	Subtotal	21,850	23,666	23,531	22,485	23,287	29,701	29,812	29,443	28,319	25,571	26,166	283,826
33.	D. Ancillary Services (Including GMC)	74,960	82,590	81,755	89,206	90,159	103,498	107,246	96,762	91,246	79,300	81,102	977,824
34.	Subtotal (A + B + C + D)	364,305	378,492	402,323	393,393	404,895	437,157	429,073	416,581	416,194	390,735	391,155	4,424,304
35.	Current Month (Over)/UnderCollection	(49,504)	(68,552)	(18,137)	(50,065)	(106,009)	(175,047)	(255,792)	(202,758)	(155,478)	(50,410)	(48,992)	(1,180,744)
36.	Accumulated UnderCollections	-	-	-	-	-	-	-	-	-	-	-	-
37.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-
38.	**California Procurement Adjustment**	**(49,504)**	**(68,552)**	**(18,137)**	**(50,065)**	**(106,009)**	**(175,047)**	**(255,792)**	**(202,758)**	**(155,478)**	**(50,410)**	**(48,992)**	**(1,180,744)**

NOTE: All assumptions are listed on the attached sheet.

Est. Net Short GWh (Feb through Dec)	21,171
CPA/Est. Net Short (GWh)	$55.77

Attachment B

1. QF Payments @ $80/MWh

Southern California Edison Company
Calculation of California Procurement Adjustment
(As Set Forth in ABX1)
(Unless Denoted Otherwise, Amounts are in Thousands)

Line No.	Component	2002 Estimate January	February	March	April	May	June	July	August	September	October	November	December	Total
1.	Total Delivered Sales (Metered GWh)	6,939	6,352	6,904	6,406	6,705	7,335	7,506	8,395	7,772	7,607	6,886	6,732	85,540
2.	Generation Rate As of 1-05-01 ($/MWh)	61.38	61.38	61.38	61.38	61.38	68.03	78.01	78.01	78.01	71.36	61.38	61.38	67.44
3.	Emergency Procurement Surcharge ($/MWh)	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
4.	Generation Rate + EPS ($/MWh)	71.38	71.38	71.38	71.38	71.38	78.03	88.01	88.01	88.01	81.36	71.38	71.38	77.44
5.	Gross Generation Revenue	(495,336)	(453,394)	(492,779)	(457,284)	(478,598)	(572,393)	(660,632)	(738,809)	(684,057)	(618,904)	(491,549)	(480,499)	(6,624,234)
Adjustments:														
6.	Franchise Fees and Uncollectibles	5,556	5,086	5,528	5,129	5,368	6,421	7,410	8,287	7,673	6,942	5,514	5,390	74,304
7.	Direct Access Credit	46,039	42,141	45,802	42,503	44,484	53,201	61,403	68,669	63,580	57,524	45,687	44,660	615,693
8.	RMR	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	3,296	39,551
9.	Restructuring Implementation	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	2,800	33,606
10.	Other Authorized Costs/Credits	7,266	7,236	7,205	7,174	7,143	7,112	7,081	7,050	7,019	6,988	6,957	6,926	85,157
11.	Imputed 10% Rate Reduction	-	-	-	-	-	-	-	-	-	-	-	-	-
12.	Imputed TTA	-	-	-	-	-	-	-	-	-	-	-	-	-
13.	**Generation-Related Component**	**(430,378)**	**(392,835)**	**(428,149)**	**(396,382)**	**(415,506)**	**(499,562)**	**(578,641)**	**(648,706)**	**(599,688)**	**(541,353)**	**(427,295)**	**(417,427)**	**(5,775,923)**
14.	Generation-Related Rate ($/MWh)	68.45	68.26	68.45	68.29	68.40	75.17	85.09	85.29	85.16	78.55	68.49	68.44	74.53
Less:														
15.	A. SCE Owned Generation Rev Rqmt:													
16.	Capital Related	23,660	23,660	23,660	23,660	23,660	23,660	23,656	23,655	23,655	23,653	23,654	23,654	283,891
17.	SONGS ICIP	49,966	45,126	49,966	36,711	24,198	48,352	49,966	49,966	48,352	33,354	27,599	49,922	513,477
18.	Other On-Going (PV, Coal, and Hydro)	52,609	34,628	32,950	25,570	32,687	34,870	37,147	38,246	36,873	36,093	38,298	38,415	438,384
19.	Subtotal	126,235	103,415	106,576	85,941	80,545	106,882	110,769	111,867	108,880	93,101	89,551	111,991	1,235,752
20.	B. QF Payments:													
21.	QF Energy and Capacity Costs	171,840	172,480	156,480	174,080	169,680	177,440	171,760	173,680	171,680	165,280	170,640	164,480	2,039,520
22.	QF Buyouts	9,404	3,587	7,024	9,404	3,587	6,119	8,498	2,681	6,119	8,498	2,681	6,119	73,721
23.	Shareholder Incentives	-	-	-	-	-	-	-	-	-	-	-	-	-
24.	Scheduling, Dispatch & Admin	70	70	70	70	70	70	70	70	70	70	70	70	840
25.	Subtotal	181,314	176,137	163,574	183,554	173,337	183,629	180,328	176,431	177,869	173,848	173,391	170,669	2,114,081
26.	C. Bilateral Contract Costs:													
27.	Interutility Net Contract Costs	14,051	13,375	13,262	13,487	11,862	13,044	14,966	14,989	15,559	15,880	13,757	13,979	168,211
28.	Interutility Buyouts	-	-	-	-	-	-	-	-	-	-	-	-	-
29.	Scheduling, Dispatch & Admin	262	262	262	262	262	262	262	262	262	262	262	262	3,139
30.	BFM Contracts Costs	-	-	-	-	-	-	-	-	-	-	-	-	-
31.	Bilateral Contract Costs	5,184	4,707	5,184	5,057	5,184	5,009	5,184	5,232	4,961	5,232	5,009	5,136	61,079
32.	Subtotal	19,497	18,344	18,708	18,806	17,308	18,315	20,412	20,483	20,782	21,374	19,028	19,377	212,932
33.	D. Ancillary Services (Including GMC)	47,553	43,380	48,664	46,758	50,996	53,917	59,438	62,351	56,914	52,208	46,968	46,943	616,090
34.	Subtotal (A + B + C + D)	374,598	341,275	337,521	335,058	322,186	362,743	370,946	371,132	364,445	340,531	328,937	348,980	4,198,353
35.	Current Month (Over)/UnderCollection	(55,781)	(51,559)	(90,628)	(61,324)	(93,320)	(136,819)	(207,695)	(277,574)	(235,243)	(200,822)	(98,357)	(68,447)	(1,577,570)
36.	Accumulated UnderCollections	-	-	-	-	-	-	-	-	-	-	-	-	-
37.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-	-
38.	**California Procurement Adjustment**	**(55,781)**	**(51,559)**	**(90,628)**	**(61,324)**	**(93,320)**	**(136,819)**	**(207,695)**	**(277,574)**	**(235,243)**	**(200,822)**	**(98,357)**	**(68,447)**	**(1,577,570)**

NOTE: All assumptions are listed on the attached sheet.

Est. Net Short GWh	27,027
CPA/Est. Net Short (GWh)	$58.37

Attachment C

Pacific Gas and Electric Company
Calculation of California Procurement Adjustment
(As Set Forth in AB1X)
($000s)

Scenario 1: QF at $80/MwH

Line No.	Component	Estimated											
		February	March	April	May	June	July	August	September	October	November	December	Total
1.	Sales (Metered)	6,454	6,538	6,354	6,420	6,846	7,272	7,572	7,670	6,936	6,405	6,770	75,238
2.	Generation Rate As of 1-05-01 /1	50.03	48.70	47.80	53.85	60.51	60.51	60.42	60.40	60.92	54.22	49.58	55.44
3.	Emergency Procurement Surcharge	9.75	9.75	9.75	9.75	9.75	9.75	9.75	9.75	9.75	9.75	9.75	9.75
4.	Generation Rate + EPS	59.78	58.45	57.55	63.60	70.26	70.26	70.17	70.15	70.67	63.97	59.33	65.19
5.	Gross Generation Revenue	(385,828)	(382,130)	(365,689)	(408,329)	(480,986)	(510,900)	(531,344)	(538,068)	(490,191)	(409,732)	(401,668)	(4,904,865)
Adjustments:													
6.	Franchise Fees and Uncollectibles	3,731	3,695	3,536	3,948	4,651	4,940	5,138	5,203	4,740	3,962	3,884	47,425
7.	Direct Access Credit /2	36,266	35,919	34,372	38,382	45,210	48,022	49,945	50,580	46,078	38,514	37,754	461,042
8.	RMR /3	0	0	0	0	0	0	0	0	0	0	0	0
9.	Restructuring Implementation	0	0	0	0	0	0	0	0	0	0	0	0
10.	Remaining Transition Costs/Credits	9,366	10,447	10,724	25,312	30,903	16,099	13,197	14,298	14,403	15,011	2,821	162,581
11.	Imputed 10% Rate Reduction	(36,309)	(34,717)	(32,148)	(33,063)	(37,508)	(40,553)	(42,451)	(42,315)	(38,664)	(34,703)	0	(372,431)
12.	Imputed FTA	(32,575)	(31,349)	(29,259)	(28,462)	(30,511)	(32,896)	(34,378)	(34,246)	(31,443)	(29,875)	0	(314,995)
13.	**Generation-Related Component**	**(405,349)**	**(398,135)**	**(378,464)**	**(402,213)**	**(468,242)**	**(515,288)**	**(539,893)**	**(544,549)**	**(495,077)**	**(416,823)**	**(357,209)**	**(4,921,243)**
Less:													
14.	A. PG&E Owned Generation Rev Rqmt:												
15.	A1. Hydro												
16.	2001 Revenue Requirement /4	33,351	33,386	33,351	33,295	33,045	33,661	33,352	33,067	33,021	33,021	33,021	365,571
17.	A2. Fossil												
18.	2001 Revenue Requirement /4	18,198	30,354	15,734	16,827	19,020	20,161	19,900	19,685	18,296	17,745	17,244	213,165
19.	A3. Nuclear												
20.	Diablo ICIP	48,678	53,862	50,332	27,049	50,404	53,862	53,862	52,134	53,934	52,134	53,862	550,115
21.	CCFT Credit	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(3,783)	(41,613)
22.	Subtotal	44,895	50,079	46,549	23,266	46,621	50,079	50,079	48,351	50,151	48,351	50,079	508,502
23.	Subtotal (A1 + A2 + A3)	96,443	113,819	95,634	73,389	98,686	103,901	103,331	101,104	101,469	99,118	100,345	1,087,239
24.	B. QF Payments												
25.	QF Expenses	124,218	128,629	127,371	144,072	152,047	155,793	153,613	144,032	140,423	128,515	141,331	1,540,043
26.	QF Admin & Legal Costs	759	759	759	759	759	759	759	759	759	759	759	8,349
27.	Subtotal	124,977	129,388	128,130	144,831	152,806	156,552	154,372	144,791	141,182	129,274	142,090	1,548,392
28.	C. Bilateral Contract Costs:												
29.	Irrigation District Contracts and Other /5	(12,202)	(10,681)	(7,140)	1,112	7,360	280	(5,639)	(9,151)	(10,572)	(4,272)	1,544	(49,362)
30.	BFM Contracts Costs /6	0	0	0	0	0	0	0	0	0	0	0	0
31.	Bilateral Contract Costs	8,904	8,349	6,503	6,763	6,763	23,129	23,753	22,321	22,349	21,335	21,829	171,998
32.	Subtotal	(3,298)	(2,332)	(637)	7,875	14,123	23,409	18,114	13,170	11,777	17,063	23,373	122,636
33.	D. ISO Ancillary Services and Related Charges /7	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	20,000	220,000
34.	Subtotal (A + B + C + D)	238,121	260,876	243,127	246,095	285,614	303,861	295,817	279,065	274,427	265,455	285,808	2,978,267
35.	Current Month (Over)/UnderCollection	(167,228)	(137,259)	(135,337)	(156,118)	(182,628)	(211,427)	(244,076)	(265,484)	(220,650)	(151,369)	(71,401)	(1,942,976)
36.	Accumulated UnderCollections	0	0	0	0	0	0	0	0	0	0	0	0
37.	Interest (6.5% Short-Term) if Undercollection	0	0	0	0	0	0	0	0	0	0	0	0
38.	**California Procurement Adjustment**	**(167,228)**	**(137,259)**	**(135,337)**	**(156,118)**	**(182,628)**	**(211,427)**	**(244,076)**	**(265,484)**	**(220,650)**	**(151,369)**	**(71,401)**	**(1,942,976)**

Net Short GWh (Feb through Dec)	32,927
Contribution to Net Short ($/MWh)	$59.01

Attachment D

San Diego Gas & Electric Company
Calculation of California Procurement Adjustment for AB 265 Customers
(As Set Forth in ABX1)

Line No.	Component ($000)	2001 Estimate February	March	April	May	June	July	August	September	October	November	December	Total
1.	Delivered Sales (GWH) /1	903	878	848	831	880	976	1,009	1,094	943	892	937	10,192
2.	AB 265 Capped Generation Rate ($/MWH)	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00
3.	Gross Generation Revenue	(58,673)	(57,093)	(55,127)	(54,031)	(57,191)	(63,414)	(65,608)	(71,105)	(61,291)	(57,996)	(60,930)	(662,458)
Adjustments:													
4.	Franchise Fees and Uncollectibles	835	733	701	683	727	808	961	998	765	676	689	8,576
5.	**Generation-Related Component**	**(57,838)**	**(56,360)**	**(54,426)**	**(53,348)**	**(56,464)**	**(62,605)**	**(64,648)**	**(70,107)**	**(60,526)**	**(57,320)**	**(60,241)**	**(653,882)**
Less:													
6.	A. SDG&E Owned Generation Rev Rqmt:												
7.	SONGS ICIP	6,525	9,801	9,338	9,540	9,179	9,595	9,718	9,471	9,595	9,298	9,869	101,929
8.	B. QF Payments:												
9.	QF Energy and Capacity Costs	13,648	10,549	8,231	10,816	11,008	12,162	13,098	12,667	8,281	7,903	8,368	116,731
10.	C. Bilateral Contract Costs:												
11.	Interutility Net Contract Costs (PNM & PGE)	3,557	3,727	6,285	2,429	2,432	2,682	2,717	2,722	2,682	2,672	2,759	34,663
12.	Bilateral Contracts	3,867	4,256	4,028	4,119	3,983	4,119	4,220	4,062	4,166	4,011	4,237	45,068
13.	Subtotal	7,424	7,982	10,314	6,548	6,414	6,802	6,936	6,784	6,848	6,683	6,996	79,732
14.	D. Ancillary Services (including GMC)	8,730	9,287	8,806	8,591	9,427	10,430	17,226	10,216	8,282	6,340	7,676	105,011
15.	E. Purchased Electric Commodity Account (PECA)	12,696	12,591	12,397	12,256	12,185	12,326	12,485	12,573	12,326	12,344	12,679	136,858
16.	Subtotal (A + B + C + D + E)	49,024	50,209	49,086	47,751	48,213	51,314	59,464	51,710	45,333	42,568	45,588	540,260
17.	Current Month (Over)/UnderCollection	(8,814)	(6,151)	(5,340)	(5,597)	(8,251)	(11,292)	(5,184)	(18,396)	(15,193)	(14,751)	(14,653)	(113,622)
18.	Accumulated UnderCollections	(8,814)	(6,151)	(5,340)	(5,597)	(8,251)	(11,292)	(5,184)	(18,396)	(15,193)	(14,751)	(14,653)	(113,622)
19.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-
20.	**California Procurement Adjustment**	**(8,814)**	**(6,151)**	**(5,340)**	**(5,597)**	**(8,251)**	**(11,292)**	**(5,184)**	**(18,396)**	**(15,193)**	**(14,751)**	**(14,653)**	**(113,622)**

Est. Net Short GWH (Feb. through Dec.)	6,178
CPA / Est. Net Short ($/MWH)	18.39

FOOTNOTES: 1/ Represents Utility Bundled Sales. The approximate split between AB265 Capped and Non-AB265 Customers is 70 / 30. Direct Access is not included because the CPUC has not yet approved cap plementation for them.

2/ The California Procurement Adjustment amount calculated above reflects the monthly amount available to the DWR for procuring power for utility customers, including the cost of imbalance energy and imbalance penalties.

Attachment D

San Diego Gas & Electric Company
Calculation of California Procurement Adjustment for AB 265 Customers
(As Set Forth In ABX1)

Line No.	Component ($000)	2002 Estimate January	February	March	April	May	June	July	August	September	October	November	December	Total
1.	Delivered Sales (GWH)	971	904	882	858	840	891	992	1,030	1,118	962	910	957	11,314
2.	AB 265 Capped Generation Rate ($/MWH)	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00	65.00
3.	Gross Generation Revenue	(63,112)	(58,771)	(57,328)	(55,739)	(54,608)	(57,911)	(64,507)	(66,923)	(72,679)	(62,507)	(59,120)	(62,228)	(735,434)
Adjustments:														
4.	Franchise Fees and Uncollectibles	696	614	595	578	567	630	745	841	879	703	611	625	8,082
5.	**Generation-Related Component**	**(62,416)**	**(58,157)**	**(56,733)**	**(55,161)**	**(54,041)**	**(57,281)**	**(63,763)**	**(66,082)**	**(71,800)**	**(61,805)**	**(58,510)**	**(61,603)**	**(727,351)**
Less:														
6.	A. SDG&E Owned Generation Rev Rqmt:													
7.	SONGS ICIP	9,929	8,809	9,685	9,242	8,498	4,453	8,092	9,617	9,373	5,436	8,738	9,753	101,625
8.	B. QF Payments:													
9.	QF Energy and Capacity Costs	6,274	6,163	6,120	6,034	8,927	8,875	8,991	9,106	9,171	6,000	6,000	6,163	87,825
10.	C. Bilateral Contract Costs:													
11.	Interutility Net Contract Costs (PNM & PGE)	2,820	2,726	2,751	2,698	2,435	2,438	2,699	2,734	2,738	2,699	2,685	2,772	32,194
12.	Bilateral Contracts	3,479	3,094	3,394	3,250	3,303	3,176	3,327	3,384	3,268	3,341	3,218	3,403	39,638
13.	Subtotal	6,299	5,820	6,144	5,948	5,738	5,614	6,026	6,118	6,006	6,040	5,902	6,175	71,832
14.	D. Ancillary Services (including GMC)	6,069	5,039	5,445	4,724	4,925	6,421	8,829	11,417	8,801	5,548	4,600	5,115	76,931
15.	E. Purchased Electric Commodity Account (PECA)	-	-	-	-	-	-	-	-	-	-	-	-	-
16.	Subtotal (A + B + C + D +E)	28,572.31	25,830.95	27,394.55	25,947.71	28,088.41	25,363.41	31,937.72	36,258.38	33,350.41	23,022.12	25,240.61	27,206.11	338,213
17.	Current Month (Over)/UnderCollection	(33,844)	(32,326)	(29,339)	(29,213)	(25,952)	(31,918)	(31,825)	(29,823)	(38,450)	(38,782)	(33,269)	(34,397)	(389,138)
18.	Accumulated UnderCollections	(33,844)	(32,326)	(29,339)	(29,213)	(25,952)	(31,918)	(31,825)	(29,823)	(38,450)	(38,782)	(33,269)	(34,397)	(389,138)
19.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-	-
20.	**California Procurement Adjustment**	**(33,844)**	**(32,326)**	**(29,339)**	**(29,213)**	**(25,952)**	**(31,918)**	**(31,825)**	**(29,823)**	**(38,450)**	**(38,782)**	**(33,269)**	**(34,397)**	**(389,138)**

Est. Net Short GWH (Feb. through Dec.)	7,223
CPA / Est. Net Short ($/MWH)	53.87

FOOTNOTES 1/ Represents Utility Bundled Sales. The approximate split between AB265 Capped and Non-AB265 Customers is 70 / 30. Direct Access is not included because the CPUC has not yet approved cap plementation for them.

2/ The California Procurement Adjustment amount calculated above reflects the monthly amount available to the DWR for procuring power for utility customers, including the cost of imbalance energy and imbalance penalties.

Attachment D

San Diego Gas & Electric Company
Calculation of California Procurement Adjustment for Uncapped Customers
(As Set Forth in ABX1)

Line No.	Component ($000)	2001 Estimate February	March	April	May	June	July	August	September	October	November	December	Total
1.	Total Delivered Sales (GWH)	351	352	358	365	393	420	416	440	406	382	366	4,251
2.	Projected Uncapped Generation Rate ($/MWH)	156.52	126.52	123.90	122.17	123.77	124.57	165.59	152.35	118.92	100.91	93.43	128.06
3.	Gross Generation Revenue	(54,944)	(44,515)	(44,395)	(44,566)	(48,697)	(52,333)	(68,933)	(67,083)	(48,286)	(38,588)	(34,230)	(546,570)
Adjustments:													
4.	Franchise Fees and Uncollectibles	325	294	296	300	325	348	396	402	330	290	269	3,574
5.	**Generation-Related Component**	**(54,620)**	**(44,221)**	**(44,099)**	**(44,266)**	**(48,372)**	**(51,985)**	**(68,537)**	**(66,681)**	**(47,956)**	**(38,299)**	**(33,960)**	**(542,996)**
Less:													
6.	A. SDG&E Owned Generation Rev Rqmt:												
7.	SONGS ICIP	2,538	3,926	3,945	4,186	4,105	4,132	4,008	3,812	4,132	3,985	3,857	42,625
8.	B. QF Payments:												
9.	QF Energy and Capacity Costs	5,308	4,225	3,477	4,747	4,922	5,237	5,402	5,099	3,566	3,387	3,270	48,641
10.	C. Bilateral Contract Costs:												
11.	Interutility Net Contract Costs (PNM & PGE)	1,383	1,493	2,655	1,066	1,087	1,155	1,120	1,096	1,155	1,145	1,078	14,434
12.	Bilateral Contracts	1,504	1,705	1,702	1,808	1,781	1,774	1,740	1,635	1,794	1,719	1,656	18,817
13.	Subtotal	2,887	3,197	4,357	2,874	2,868	2,929	2,861	2,731	2,949	2,864	2,734	33,251
14.	D. Ancillary Services (including GMC)	3,395	3,720	3,720	3,770	4,216	4,491	7,104	4,112	3,566	2,717	3,000	43,812
15.	Subtotal (A + B + C + D)	14,127	15,068	15,500	15,577	16,111	16,789	19,375	15,754	14,213	12,953	12,862	168,330
16.	Current Month (Over)/UnderCollection	(40,492)	(29,153)	(28,599)	(28,689)	(32,261)	(35,196)	(49,162)	(50,927)	(33,743)	(25,345)	(21,099)	(374,666)
17.	Accumulated UnderCollections	(40,492)	(29,153)	(28,599)	(28,689)	(32,261)	(35,196)	(49,162)	(50,927)	(33,743)	(25,345)	(21,099)	(374,666)
18.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-
19.	**California Procurement Adjustment**	(40,492)	(29,153)	(28,599)	(28,689)	(32,261)	(35,196)	(49,162)	(50,927)	(33,743)	(25,345)	(21,099)	(374,666)

Est. Net Short GWH (Feb. through Dec.) 2,578
CPA / Est. Net Short ($/MWH) 145.35

FOOTNOTES 1/ Represents Utility Bundled Sales. The approximate split between AB265 Capped and Non-AB265 Customers is 70 / 30. Direct Access is not included because the CPUC has not yet approved cap plementation for them.

2/ The California Procurement Adjustment amount calculated above reflects the monthly amount available to the DWR for procuring power for utility customers, including the cost of imbalance energy and imbalance penalties.

Attachment D

San Diego Gas & Electric Company
Calculation of California Procurement Adjustment for Uncapped Customers
(As Set Forth in ABX1)

Line No.	Component ($000)	2002 Estimate January	February	March	April	May	June	July	August	September	October	November	December	Total
1.	Delivered Sales (GWH)	355	353	353	361	369	398	425	423	448	412	390	374	4,662
2.	Projected Uncapped Generation Rate ($/MWH)	87.19	74.83	73.12	73.03	73.32	83.98	98.43	120.70	110.25	91.94	72.07	65.91	74.83
3.	Gross Generation Revenue	(30,995)	(26,444)	(25,831)	(26,330)	(27,032)	(33,457)	(41,863)	(51,005)	(49,378)	(37,891)	(28,095)	(24,662)	(402,982)
Adjustments:														
4.	Franchise Fees and Uncollectibles	255	240	238	243	249	282	319	345	352	301	262	244	3,330
5.	**Generation-Related Component**	(30,740)	(26,204)	(25,593)	(26,087)	(26,783)	(33,175)	(41,543)	(50,660)	(49,026)	(37,589)	(27,833)	(24,418)	(399,652)
Less:														
6.	A. SDG&E Owned Generation Rev Rqmt:													
7.	SONGS ICIP	3,635	3,443	3,880	3,886	3,730	1,991	3,468	3,947	3,754	2,330	3,745	3,812	41,620
8.	B. QF Payments:													
9.	QF Energy and Capacity Costs	2,297	2,409	2,451	2,537	3,917	3,969	3,853	3,738	3,673	2,571	2,571	2,409	36,396
10.	C. Bilateral Contract Costs:													
11.	Interutility Net Contract Costs (PNM & PGE)	1,032	1,065	1,102	1,134	1,068	1,090	1,157	1,122	1,097	1,157	1,151	1,083	13,259
12.	Bilateral Contracts	1,274	1,209	1,359	1,366	1,450	1,420	1,426	1,389	1,309	1,432	1,379	1,330	16,344
13.	Subtotal	2,306	2,275	2,461	2,501	2,518	2,510	2,583	2,511	2,406	2,589	2,530	2,413	29,603
14.	D. Ancillary Services (including GMC)	2,222	1,969	2,181	1,986	2,161	2,872	3,784	4,686	3,525	2,377	1,972	1,999	31,734
15.	Subtotal (A + B + C + D)	10,460.90	10,095.27	10,973.17	10,909.83	12,326.57	11,341.96	13,687.60	14,881.79	13,358.85	9,866.62	10,817.40	10,632.71	139,353
16.	Current Month (Over)/UnderCollection	(20,279)	(16,109)	(14,620)	(15,178)	(14,456)	(21,833)	(27,856)	(35,778)	(35,667)	(27,723)	(17,016)	(13,785)	(260,300)
17.	Accumulated UnderCollections	(20,279)	(16,109)	(14,620)	(15,178)	(14,456)	(21,833)	(27,856)	(35,778)	(35,667)	(27,723)	(17,016)	(13,785)	(260,300)
18.	Interest (6.5% Short-Term)	-	-	-	-	-	-	-	-	-	-	-	-	-
19.	**California Procurement Adjustment**	(20,279)	(16,109)	(14,620)	(15,178)	(14,456)	(21,833)	(27,856)	(35,778)	(35,667)	(27,723)	(17,016)	(13,785)	(260,300)

Est. Net Short GWH (Feb. through Dec.)	2,986
CPA / Est. Net Short ($/MWH)	87.18

FOOTNOTES 1/ Represents Utility Bundled Sales. The approximate split between AB265 Capped and Non-AB265 Customers is 70 / 30. Direct Access is not included because the CPUC has not yet approved cap plementation for them.

2/ The California Procurement Adjustment amount calculated above reflects the monthly amount available to the DWR for procuring power for utility customers, including the cost of imbalance energy and imbalance penalties.

Attachment E
Based on Utility Provided Scenarios, 12 month Projections for 2001

	A	B	C	D	E	F	G	H	I
	Total Generation Related Rate (¢/kWh)	Sales Reported in Utilities' ABX1 Data (GWh)	Bundled Service Sales (GWh)	Gross Gen. - Related Revs Reported in Utilities' ABX1 Data ($000s)	Gen. - Related Revenues Based on Bundled Service Sales ($000s)	Utility Related Costs ($000s)	Utility Related Costs less CSI and A&G ($000s)	CPA Revenues ($000s)	CPA Rate (¢/kWh)
	A=D/B/10				E=A*C*10			H=E-G	I=H/C
PG&E	6.471	82,008	74,299	$5,306,533	$4,807,719	$3,264,075	$3,188,127	$1,619,592	2.180
SCE	7.277	84,400	76,466	$6,141,557	$5,564,251	$4,798,902	$4,762,381	$801,870	1.049
SDGE Capped	6.500	11,163	11,163	$725,570	$725,570	$431,974	$431,974	$293,596	2.630
SDGE Uncapped	12.539	4,606	4,606	$577,565	$577,565	$178,791	$178,791	$398,774	8.658
Totals				$12,751,225	$11,675,105	$8,673,742	$8,561,273	$3,113,832	

Notes

Column A: Calculated based on gross generation-related revenues shown in column D and sales shown in column B.

Column B: Based on Utilities' sales data provided in ABX1 implementation worksheets emailed to parties in A.00-11-038, et.al, on 2-9-01.
PG&E: Scenario 1: (QFs at $80/MWh); Total metered sales for 2/'01 thru 12/'01 (75,238 GWh), plus 12/'01 sales (6,770 GWh) for 12th month.
SCE: Scenario with QFs at $80/MWh: Total metered sales for 2/'01 thru 12/'01 (77,461 GWh), plus 1/'02 sales (6,939 GWh) for 12th mo.
SDG&E: Total delivered sales for 2/'01 thru 12/'01 (10,192 GWH for capped; 4,251 GWh for uncapped), plus 1/'02 sales (971 GWh for capped; 355 GWh for uncapped) for 12th mo.

Column C: PG&E & SCE: Column B x 0.906 to remove sales to direct access customers.

Column D: Based on Utilities' sales data provided in ABX1 implementation worksheets emailed to parties in A.00-11-038, et.al, on 2-9-01.
PG&E: Scenario 1: (QFs at $80/MWh); Gross generation revenue for 2/'01 thru 12/'01 ($4,904,865), plus 12/'01 revenue ($401,668) for 12th month.
SCE: Scenario with QFs at $80/MWh: Gross generation revenue for 2/'01 thru 12/'01 ($5,685,772), plus 1/'02 revenue ($495,336) for 12th mo. less RMR ($36,255 for Feb. '01 thru Dec. '02, plus $3,296 for Jan. '02).
SDG&E: Total delivered sales for 2/'01 thru 12/'01 ($662,458 for capped; $546,470 for uncapped), plus 1/'02 revenues ($63,112 for capped; $30,995 for uncapped) for 12th mo.

Column E: Calculated based on total generation rate shown in Column A and bundled service sales shown in column C.

Column F: Based on Utilities' sales data provided in ABX1 implementation worksheets emailed to parties in A.00-11-038, et.al, on 2-9-01.
PG&E: Scenario 1: (QFs at $80/MWh); Costs for PG&E-owned gen., QFs, Bilaterals, and Ancillary Services for 2/'01 thru 12/'01 ($2,978,267), plus 12/'01 costs ($285,808) for 12th month.
SCE: Scenario with QFs at $80/MWh: Costs for SCE-owned gen., QFs, Bilaterals, and Ancillary Services for 2/'01 thru 12/'01 ($4,424,304), plus 1/'02 costs ($374,598) for 12th mo.
SDG&E: Cost for SDG&E-owned gen., QFs, Bilaterals, and Ancillary Services, excluding PECA amoritzation for 2/'01 thru 12/'01 ($403,402 for capped; $168,330 for uncapped) plus 1/'02 costs ($28,572 for capped; $10,461 for capped) for 12th mo.

Column G: Column F less Customer Service and Information, and A&G costs identified in utilities data supporting ABX1 implementation worksheets.
PG&E: Column F minus $75,948; SCE: Column F minus $36,521.

A.00-11-038 et al.
D.01-03-081

Commissioner Richard A. Bilas, concurring:

Absent today's tandem rate increase order, D.01-03-082, I would have voted no on this order. Since I voted for the rate increase, I feel more comfortable requiring the utilities to begin paying Department of Water Resources (DWR). However, I still have reservations about adopting a formula that requires the utilities to devote a revenue stream to DWR outside a CPA calculation. It is not clear to me that the Legislature, in adopting AB 1X, intended such a result. To my mind it raises the specter of the now rescinded portions of our January order under SB 7x, D.00-01-061, which we had to modify in D.01-02-077. We did not take public comment on that order. We did not take public comment on this order. Acting in a vacuum is dangerous. Acting in a vacuum and at the last minute is foolhardy.

For example, changes in the tandem rate increase order, made at the last minute before today's meeting, reach back into this order. They state that the 3 cents per kilowatt hour will be added on top of the company wide average generation rates for Southern California Edison Company and Pacific Gas and Electric Company. This decision adopted the company wide average generation rates based on an evidentiary record. I do not think it wise to just lump the 3 cents on top of the 7.277 and 6.471 cents, respectively, without a record. We should instead direct that the calculation for inclusion of the 3 cents should be part of those details we plan to work out later. Treatment of the three cents is especially important to assess in light of the interim CPA we will adopt at the continuation meeting on April 3, 2001. We at least had final oral argument on the tandem ALJ's proposed rate stabilization decision and President Lynch's alternate decision that raises rates. We had little time for consideration and no comment or oral argument on this order.

While I voted in favor of this decision, I did so relying on the order's statement that we will work out the details on payment to DWR later. I consider those details to include a reconsideration of the incorporation of the three cents in the company wide average generation rates and a change in methodology should our haste have proven to be ill advised.

/s/ RICHARD A. BILAS
RICHARD A. BILAS
Commissioner

San Francisco, California
March 27, 2001

L/mal

MAIL DATE
MAY 16, 2001

Decision 01-05-063 May 14, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 388-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
Emergency Application of Pacific Gas and Electric Company (U 39 E) to Adopt a Rate Stabilization Plan.	Application 00-11-056 (Filed November 22, 2000)
Petition of The Utility Reform Network for Modification of Resolution E-3527.	Application 00-10-028 (Filed October 17, 2000)

ORDER DENYING REHEARING OF DECISION (D.) 01-04-005

On May 4, 2001 CE Generation applied for rehearing of Decision (D.) 01-04-005. This decision adopts a method for calculating the California Procurement Adjustment (CPA) contemplated by Public Utilities Code section 360.5,[1] and then calculates the CPA rate for each electric utility. The decision also concludes that the order constitutes a financing order under Water Code section 80110.

Section 1731(b)[2] requires that a party file an application for rehearing "within 30 days after the date of issuance or within 10 days after the date of issuance in the case of an order issued pursuant to either Article 5 (commencing with Section 816) or

[1] Unless otherwise noted, all statutory references herein are to the Public Utilities Code.

[2] CE Generation refers to section 1730 as authority for filing its rehearing application. Since no such section exists, we refer to section 1731, which does apply to filing of rehearing applications.

Certified as a True Copy
of the Original
EXECUTIVE DIRECTOR, PUBLIC UTILITIES COMM.

Article 6 (commencing with Section 851) of Chapter 4 relating to security transactions and the transfer or encumbrance of utility property." AB 1X authorizes the Commission to enter into an agreement with the Department of Water Resources (DWR) that "shall have the force and effect of a financing order adopted in accordance with Article 5.5 (commencing with Section 840) of Chapter 4 of Part 1 of Division 1 of the Public Utilities Code, as determined by the commission." (Water Code § 80110.)

Decision 01-04-005 relates to the issuance of bonds, i.e. security transactions. As discussed in Decision (D.) 01-05-037, the order denying the rehearing applications of Pacific Gas and Electric Company (PG&E) and Southern California Edison Company (Edison) of D.01-04-005, setting the CPA will determine DWR's maximum legal bonding authority. Thus D.01-04-005 requires the degree of certainty and level of urgency specified in section 1731 and is subject to the 10-day deadline for filing rehearing applications.

CE Generation filed its rehearing application on May 4, 2001. This is after the 10-day deadline. Accordingly, its application is untimely and is denied.

Furthermore, all the arguments raised by CE Generation were raised by PG&E and Edison in their rehearing applications of D.01-04-005 filed on April 16, 2001. These arguments were all addressed in Decision (D.) 01-05-037, our order denying PG&E's and Edison's rehearing applications. Accordingly, even if this application were timely, it would have been denied for the reasons stated in D.01-05-037.

Therefore **IT IS ORDERED** that the rehearing application of CE Generation is denied.

This order is effective today.

Dated May 14, 2001, at San Francisco, California.

LORETTA M. LYNCH
President
RICHARD A. BILAS
HENRY M. DUQUE
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners

L/mal

MAIL DATE
MAY 16, 2001

Decision 01-05-063 May 14, 2001

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (U 388-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
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Decision 01-04-005 relates to the issuance of bonds, i.e. security transactions. As discussed in Decision (D.) 01-05-037, the order denying the rehearing applications of Pacific Gas and Electric Company (PG&E) and Southern California Edison Company (Edison) of D.01-04-005, setting the CPA will determine DWR's maximum legal bonding authority. Thus D.01-04-005 requires the degree of certainty and level of urgency specified in section 1731 and is subject to the 10-day deadline for filing rehearing applications.

CE Generation filed its rehearing application on May 4, 2001. This is after the 10-day deadline. Accordingly, its application is untimely and is denied.

Furthermore, all the arguments raised by CE Generation were raised by PG&E and Edison in their rehearing applications of D.01-04-005 filed on April 16, 2001. These arguments were all addressed in Decision (D.) 01-05-037, our order denying PG&E's and Edison's rehearing applications. Accordingly, even if this application were timely, it would have been denied for the reasons stated in D.01-05-037.

Therefore **IT IS ORDERED** that the rehearing application of CE Generation is denied.

This order is effective today.

Dated May 14, 2001, at San Francisco, California.

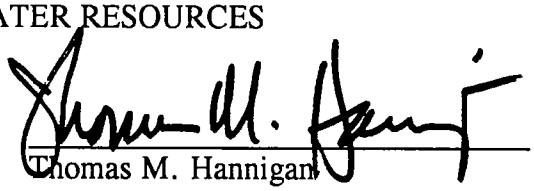
LORETTA M. LYNCH
President
RICHARD A. BILAS
HENRY M. DUQUE
CARL W. WOOD
GEOFFREY F. BROWN
Commissioners

ACCEPTANCE BY DEPARTMENT OF WATER RESOURCES
OF PUBLIC UTILITIES COMMISSION DECISIONS

The California Department of Water Resources (the "Department") hereby acknowledges that as a result of the order in Decision No. 01-03-009, dated March 7, 2001, issued by the California Public Utilities Commission (the "Commission") on March 9, 2001, and the March 5, 2001, letter from the Department to the Commission attached to the decision as Attachment B, declaring that the Department's present needs are satisfied by the decision and requesting its adoption, an agreement has been entered into between the Department and the Commission with respect to such order, as permitted by such order and Section 80110 of the California Water Code. The Department, pursuant to ordering paragraph 2 of Decision No. 01-04-005, dated April 3, 2001, issued by the Commission on April 4, 2001, hereby accepts the determination of the CPA rate and the annual revenues generated by the CPA as set forth in ordering paragraph 1 of that decision, and acknowledges that as a result, an agreement has been entered into between the Department and the Commission with respect to such matters, as permitted by Section 80110 of the California Water Code.

Dated: June 26, 2001.

CALIFORNIA DEPARTMENT OF
WATER RESOURCES

By 
Thomas M. Hannigan
Director

CERTIFICATE OF CALIFORNIA PUBLIC UTILITIES COMMISSION

The California Public Utilities Commission hereby certifies that attached hereto are true and correct copies of D.01-03-009, D.01-03-081 and D.01-04-005. On April 3, 2001, the Executive Director issued D.01-04-003 modifying D.01-03-009 to correct a clerical error, and on May 14, 2001, the Commission issued D.01-05-063 denying rehearing of D.01-04-005. True and correct copies of these two decisions are attached as well. Except as so noted, D.01-03-009, D.01-03-081 and D.01-04-005 have not been amended or modified and remain in full force and effect, and the Commission acknowledges receipt of an acceptance dated June 26, 2001, of the California Department Water Resources pursuant to ordering paragraph 2 of D.01-04-005.

Dated: June 26, 2001.

CALIFORNIA PUBLIC
UTILITIES COMMISSION

By Wesley M. Franklin.
Name: Wesley M. Franklin
Title: Executive Director

THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND.

PROMISSORY NOTE

$500,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Commerzbank Aktiengesellschaft, New York Branch (the "Lender"), for the account of its Lending Office (as defined in the Credit and Security Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, the Lender, the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"); capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of Five Hundred Million United States dollars ($500,000,000.00) or, if less, the unpaid principal amount of the Taxable Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Taxable Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Taxable Loan of the Lender in part, each remaining principal payment shall be reduced

SPECIMEN

downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Taxable Loan of the Lender in like money at said office from the date such Taxable Loan is made until paid in full at the rates and at the times provided in the Credit Agreement.

This Promissory Note is one of the Taxable Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001

SPECIMEN

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary and mandatory prepayment, in whole or in part, and the Taxable Loan of the Lender or portions thereof may be converted from Base Rate Loans to LIBOR Loans and vice versa to the extent provided in the Credit Agreement.

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By _____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND.

PROMISSORY NOTE

$300,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Bayerische Landesbank Girozentrale, acting through its New York Branch (the "Lender"), for the account of its Lending Office (as defined in the Credit and Security Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, the Lender, the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"), capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of Three Hundred Million United States dollars ($300,000,000.00) or, if less, the unpaid principal amount of the Taxable Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Taxable Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Taxable Loan of the Lender in part, each remaining principal payment

shall be reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Taxable Loan of the Lender in like money at said office from the date such Taxable Loan is made until paid in full at the rates and at the times provided in the Credit Agreement.

This Promissory Note is one of the Taxable Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary and mandatory prepayment, in whole or in part, and the Taxable Loan of the Lender or portions thereof may be converted from Base Rate Loans to LIBOR Loans and vice versa to the extent provided in the Credit Agreement.

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAXABLE BOND.

PROMISSORY NOTE

$1,500,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Morgan Guaranty Trust Company of New York (the "Lender"), for the account of its Lending Office (as defined in the Credit and Security Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, the Lender, the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"); capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of One Billion Five Hundred Million United States dollars ($1,500,000,000.00) or, if less, the unpaid principal amount of the Taxable Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Taxable Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Taxable Loan of the Lender in part, each remaining principal payment shall be reduced

SPECIMEN

downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Taxable Loan of the Lender in like money at said office from the date such Taxable Loan is made until paid in full at the rates and at the times provided in the Credit Agreement.

This Promissory Note is one of the Taxable Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary and mandatory prepayment, in whole or in part, and the Taxable Loan of the Lender or portions thereof may be converted from Base Rate Loans to LIBOR Loans and vice versa to the extent provided in the Credit Agreement.

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND.

PROMISSORY NOTE

$1,000,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of JPMorgan Chase & Co. (the "Lender"), for the account of its Lending Office (as defined in the Credit and Security Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, the Lender and other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"); capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of One Billion United States dollars ($1,000,000,000.00) or, if less, the unpaid principal amount of the Tax-Exempt Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Tax-Exempt Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Tax-Exempt Loan of the Lender in part, each remaining principal payment shall be reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

SPECIMEN

The Department promises also to pay interest on the unpaid principal amount of the Tax-Exempt Loan of the Lender in like money at said office from the date such Tax-Exempt Loan is made until paid in full. Prior to October 31, 2001 (the "Term Out Period Commencement Date"), interest shall accrue at a rate per annum which shall be the sum of (A) 80% of the LIBOR Index and (B) 0.75%. On and after the Term Out Period Commencement Date, interest shall accrue at the Base Rate in effect from time to time plus the Applicable Margin. Notwithstanding the foregoing, overdue principal and, to the extent permitted by law, overdue interest in respect hereof and any other overdue amount payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the otherwise applicable interest rate (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%), and during the continuance of an Event of Default or an Event of Noncompliance, this Bond and other amounts payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the interest rate in effect therefor immediately prior to the occurrence of such Event of Default or Event of Noncompliance (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%). Accrued (and theretofore unpaid) interest shall be payable, on or before the Term Out Period Commencement Date, monthly in arrears on the first Business Day of each calendar month and on the Term Out Period Commencement Date, and thereafter quarterly in arrears on the last Business Day of each March, June, September and December.

SPECIMEN

"LIBOR Index" shall mean, for any seven consecutive day period commencing on a Wednesday and ending on the following Tuesday (or, in the case of the first reset period, the eight consecutive day period commencing on June 26, 2001 and ending on July 3, 2001 (the "Initial Period")), the offered rate per annum for deposits in Dollars for a one month period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on Wednesday of the applicable seven-day period (or, in the case of the Initial Period, on Tuesday, June 26, 2001). "Base Rate" shall mean, as of any date of determination, the rate determined by the Agent to be the higher of (a) the Prime Rate (as defined in the Credit Agreement) on that date and (b) the aggregate of the Federal Funds Rate (as defined in the Credit Agreement) on that date plus 0.50%, each determined in accordance with the Credit Agreement. The "Applicable Margin" shall be 0.00% through April 30, 2002 and thereafter shall be 1.00% through October 31, 2002, and thereafter shall be 2.00%.

This Promissory Note is one of the Tax-Exempt Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the

Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001.

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary prepayment without premium or penalty, in whole or in part, upon five (5) Business Days' prior written notice, any partial prepayment to be in an aggregate principal amount of at least $50,000,000 and $5,000,000 multiples in excess thereof applied pro rata among the Loans of all Lenders. As further provided in the Credit Agreement, this Promissory Note is also subject to mandatory prepayment in the event the State or any department, agency or other political subdivision thereof issues any Water Code Bonds (as defined in the Credit Agreement) or incurs or permits to exist any other Debt payable from or secured by the Water Code Collateral, in each case other than Permitted Debt (as defined in the Credit Agreement), and in certain other events, all as more specifically described in the Credit Agreement.

The Credit Agreement permits amendment or waiver of the terms thereof by the Department, the Majority Lenders and the Agent; provided, however, that no such change, waiver, discharge or termination shall, without the consent of each Lender, (a) extend any scheduled payment date or the final maturity of any Loan or Bond, or reduce the rate or extend the time of payment of interest or fees thereon, or reduce the principal amount thereof (it being understood that a waiver of any Default, Event of Default, Noncompliance or Event of Noncompliance not declared shall not constitute such an extension, reduction or increase), (b) release any Collateral except as specifically provided in any Transaction Document, (c) amend, modify or waive the amendment provisions or certain other specified provisions of the Credit Agreement, or (d) change the percentage specified in the definition of "Majority Lenders" or "Super Majority Lenders."

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND.

PROMISSORY NOTE

$400,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Hare & Co., nominee for The Bank of New York, as custodian under the Custody Agreement relating to RIBCO Trust Series FR/RI-K1 (the "Custodian"), for the account of the Custodian to such address as the Custodian shall specify in writing to the Department; capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, Lehman Commerical Paper Inc. (the "Lender"), the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of Four Hundred Million United States dollars ($400,000,000.00) or, if less, the unpaid principal amount of the Tax-Exempt Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Tax-Exempt Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Tax-Exempt Loan of the Lender in part, each remaining principal payment shall be

reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Tax-Exempt Loan of the Lender in like money at said office from the date such Tax-Exempt Loan is made until paid in full. Prior to October 31, 2001 (the "Term Out Period Commencement Date"), interest shall accrue at a rate per annum which shall be the sum of (A) 80% of the LIBOR Index and (B) 0.75%. On and after the Term Out Period Commencement Date, interest shall accrue at the Base Rate in effect from time to time plus the Applicable Margin. Notwithstanding the foregoing, overdue principal and, to the extent permitted by law, overdue interest in respect hereof and any other overdue amount payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the otherwise applicable interest rate (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%), and during the continuance of an Event of Default or an Event of Noncompliance, this Bond and other amounts payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the interest rate in effect therefor immediately prior to the occurrence of such Event of Default or Event of Noncompliance (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%). Accrued (and theretofore unpaid) interest shall be payable, on or before the Term Out Period Commencement Date, monthly in arrears on the first Business Day of each calendar month and on the Term Out Period Commencement Date, and thereafter quarterly in arrears on the last Business Day of each March, June, September and December.

SPECIMEN

"LIBOR Index" shall mean, for any seven consecutive day period commencing on a Wednesday and ending on the following Tuesday (or, in the case of the first reset period, the eight consecutive day period commencing on June 26, 2001 and ending on July 3, 2001 (the "Initial Period")), the offered rate per annum for deposits in Dollars for a one month period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on Wednesday of the applicable seven-day period (or, in the case of the Initial Period, on Tuesday, June 26, 2001). "Base Rate" shall mean, as of any date of determination, the rate determined by the Agent to be the higher of (a) the Prime Rate (as defined in the Credit Agreement) on that date and (b) the aggregate of the Federal Funds Rate (as defined in the Credit Agreement) on that date plus 0.50%, each determined in accordance with the Credit Agreement. The "Applicable Margin" shall be 0.00% through April 30, 2002 and thereafter shall be 1.00% through October 31, 2002, and thereafter shall be 2.00%.

This Promissory Note is one of the Tax-Exempt Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the

Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001.

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary prepayment without premium or penalty, in whole or in part, upon five (5) Business Days' prior written notice, any partial prepayment to be in an aggregate principal amount of at least $50,000,000 and $5,000,000 multiples in excess thereof applied pro rata among the Loans of all Lenders. As further provided in the Credit Agreement, this Promissory Note is also subject to mandatory prepayment in the event the State or any department, agency or other political subdivision thereof issues any Water Code Bonds (as defined in the Credit Agreement) or incurs or permits to exist any other Debt payable from or secured by the Water Code Collateral, in each case other than Permitted Debt (as defined in the Credit Agreement), and in certain other events, all as more specifically described in the Credit Agreement.

SECURED

The Credit Agreement permits amendment or waiver of the terms thereof by the Department, the Majority Lenders and the Agent; provided, however, that no such change, waiver, discharge or termination shall, without the consent of each Lender, (a) extend any scheduled payment date or the final maturity of any Loan or Bond, or reduce the rate or extend the time of payment of interest or fees thereon, or reduce the principal amount thereof (it being understood that a waiver of any Default, Event of Default, Noncompliance or Event of Noncompliance not declared shall not constitute such an extension, reduction or increase), (b) release any Collateral except as specifically provided in any Transaction Document, (c) amend, modify or waive the amendment provisions or certain other specified provisions of the Credit Agreement, or (d) change the percentage specified in the definition of "Majority Lenders" or "Super Majority Lenders."

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND.

PROMISSORY NOTE

$300,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Hare & Co., nominee for The Bank of New York, as custodian under the Custody Agreement relating to RIBCO Trust Series FR/RI-K2 (the "Custodian"), for the account of the Custodian to such address as the Custodian shall specify in writing to the Department; capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, Lehman Commerical Paper Inc. (the "Lender"), the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of Three Hundred Million United States dollars ($300,000,000.00) or, if less, the unpaid principal amount of the Tax-Exempt Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Tax-Exempt Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Tax-Exempt Loan of the Lender in part, each remaining principal payment shall be

SPECIMEN

reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Tax-Exempt Loan of the Lender in like money at said office from the date such Tax-Exempt Loan is made until paid in full. Prior to October 31, 2001 (the "Term Out Period Commencement Date"), interest shall accrue at a rate per annum which shall be the sum of (A) 80% of the LIBOR Index and (B) 0.75%. On and after the Term Out Period Commencement Date, interest shall accrue at the Base Rate in effect from time to time plus the Applicable Margin. Notwithstanding the foregoing, overdue principal and, to the extent permitted by law, overdue interest in respect hereof and any other overdue amount payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the otherwise applicable interest rate (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%), and during the continuance of an Event of Default or an Event of Noncompliance, this Bond and other amounts payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the interest rate in effect therefor immediately prior to the occurrence of such Event of Default or Event of Noncompliance (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%). Accrued (and theretofore unpaid) interest shall be payable, on or before the Term Out Period Commencement Date, monthly in arrears on the first Business Day of each calendar month and on the Term Out Period Commencement Date, and thereafter quarterly in arrears on the last Business Day of each March, June, September and December.

SECURED

"LIBOR Index" shall mean, for any seven consecutive day period commencing on a Wednesday and ending on the following Tuesday (or, in the case of the first reset period, the eight consecutive day period commencing on June 26, 2001 and ending on July 3, 2001 (the "Initial Period")), the offered rate per annum for deposits in Dollars for a one month period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on Wednesday of the applicable seven-day period (or, in the case of the Initial Period, on Tuesday, June 26, 2001). "Base Rate" shall mean, as of any date of determination, the rate determined by the Agent to be the higher of (a) the Prime Rate (as defined in the Credit Agreement) on that date and (b) the aggregate of the Federal Funds Rate (as defined in the Credit Agreement) on that date plus 0.50%, each determined in accordance with the Credit Agreement. The "Applicable Margin" shall be 0.00% through April 30, 2002 and thereafter shall be 1.00% through October 31, 2002, and thereafter shall be 2.00%.

This Promissory Note is one of the Tax-Exempt Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the

Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001.

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary prepayment without premium or penalty, in whole or in part, upon five (5) Business Days' prior written notice, any partial prepayment to be in an aggregate principal amount of at least $50,000,000 and $5,000,000 multiples in excess thereof applied pro rata among the Loans of all Lenders. As further provided in the Credit Agreement, this Promissory Note is also subject to mandatory prepayment in the event the State or any department, agency or other political subdivision thereof issues any Water Code Bonds (as defined in the Credit Agreement) or incurs or permits to exist any other Debt payable from or secured by the Water Code Collateral, in each case other than Permitted Debt (as defined in the Credit Agreement), and in certain other events, all as more specifically described in the Credit Agreement.

SPECIMEN

The Credit Agreement permits amendment or waiver of the terms thereof by the Department, the Majority Lenders and the Agent; provided, however, that no such change, waiver, discharge or termination shall, without the consent of each Lender, (a) extend any scheduled payment date or the final maturity of any Loan or Bond, or reduce the rate or extend the time of payment of interest or fees thereon, or reduce the principal amount thereof (it being understood that a waiver of any Default, Event of Default, Noncompliance or Event of Noncompliance not declared shall not constitute such an extension, reduction or increase), (b) release any Collateral except as specifically provided in any Transaction Document, (c) amend, modify or waive the amendment provisions or certain other specified provisions of the Credit Agreement, or (d) change the percentage specified in the definition of "Majority Lenders" or "Super Majority Lenders."

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By:_____
Title: Director, Department of Water Resources

SPECIMEN

THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE LIMITED OBLIGATIONS OF THE DEPARTMENT OF WATER RESOURCES PAYABLE SOLELY FROM THE REVENUES AND THE COLLATERAL DESCRIBED BELOW. THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND ARE NOT A GENERAL OBLIGATION OF THE STATE OF CALIFORNIA, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES OR THE GENERAL FUND OF THE STATE OF CALIFORNIA. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE STATE OF CALIFORNIA OR THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES IS PLEDGED TO THE PAYMENT OF THE OBLIGATIONS EVIDENCED BY THIS TAX-EXEMPT BOND.

PROMISSORY NOTE

$300,000,000.00

Sacramento, California
June 26, 2001

FOR VALUE RECEIVED, THE STATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES (the "Department"), hereby promises to pay to the order of Hare & Co., nominee for The Bank of New York, as custodian under the Custody Agreement relating to RIBCO Trust Series FR/RI-K3 (the "Custodian"), for the account of the Custodian to such address as the Custodian shall specify in writing to the Department; capitalized terms used herein but not defined shall have the meanings assigned in the Credit Agreement, dated as of June 26, 2001 (as modified, supplemented, restated, replaced or amended from time to time, the "Credit Agreement"), among the Department, Lehman Commerical Paper Inc. (the "Lender"), the other financial institutions party thereto and Morgan Guaranty Trust Company of New York, as agent (the "Agent"), in lawful money of the United States of America in immediately available funds, at the Payment Office of the Agent the principal sum of Three Hundred Million United States dollars ($300,000,000.00) or, if less, the unpaid principal amount of the Tax-Exempt Loan made by the Lender pursuant to the Credit Agreement, which principal sum or amount shall be payable in eleven equal installments of principal commencing on April 30, 2002, continuing on the last Business Day of each July, October, January and April thereafter and ending on October 31, 2004; provided that if the Department has not entered into Satisfactory Purchase Contracts by March 31, 2002 which remain in full force and effect as of such date and the Sunset Date has not been extended to be a date on or after October 31, 2004 by an amendment to the Water Code, the then unpaid principal balance of the Tax-Exempt Loan of the Lender shall be paid in equal installments (but prorated for any period which is less than three months) commencing on July 31, 2002, the last Business Day of each July, October, January and April thereafter on or before the Final Payment Date and on the Final Payment Date where the "Final Payment Date" is the later of December 28, 2002 and the day preceding the date to which the Sunset Date has been so extended; provided, further, in the event the Department prepays the Tax-Exempt Loan of the Lender in part, each remaining principal payment shall be

reduced downward by the quotient obtained by dividing the amount of the prepayment by the number of remaining principal payments.

The Department promises also to pay interest on the unpaid principal amount of the Tax-Exempt Loan of the Lender in like money at said office from the date such Tax-Exempt Loan is made until paid in full. Prior to October 31, 2001 (the "Term Out Period Commencement Date"), interest shall accrue at a rate per annum which shall be the sum of (A) 80% of the LIBOR Index and (B) 0.75%. On and after the Term Out Period Commencement Date, interest shall accrue at the Base Rate in effect from time to time plus the Applicable Margin. Notwithstanding the foregoing, overdue principal and, to the extent permitted by law, overdue interest in respect hereof and any other overdue amount payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the otherwise applicable interest rate (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%), and during the continuance of an Event of Default or an Event of Noncompliance, this Bond and other amounts payable by the Department hereunder and under the Credit Agreement shall bear interest at a rate per annum equal to 2% per annum in excess of the interest rate in effect therefor immediately prior to the occurrence of such Event of Default or Event of Noncompliance (or, if no rate is in effect therefor, at a per annum rate equal to the Base Rate plus 2%). Accrued (and theretofore unpaid) interest shall be payable, on or before the Term Out Period Commencement Date, monthly in arrears on the first Business Day of each calendar month and on the Term Out Period Commencement Date, and thereafter quarterly in arrears on the last Business Day of each March, June, September and December.

Specimen

"LIBOR Index" shall mean, for any seven consecutive day period commencing on a Wednesday and ending on the following Tuesday (or, in the case of the first reset period, the eight consecutive day period commencing on June 26, 2001 and ending on July 3, 2001 (the "Initial Period")), the offered rate per annum for deposits in Dollars for a one month period which appears at 11:00 a.m., London time, on the Telerate Monitor on Telerate Screen 3750 (or such other screen as may replace screen 3750 on the Telerate Monitor for the purpose of displaying the London interbank offered rates of major banks) on Wednesday of the applicable seven-day period (or, in the case of the Initial Period, on Tuesday, June 26, 2001). "Base Rate" shall mean, as of any date of determination, the rate determined by the Agent to be the higher of (a) the Prime Rate (as defined in the Credit Agreement) on that date and (b) the aggregate of the Federal Funds Rate (as defined in the Credit Agreement) on that date plus 0.50%, each determined in accordance with the Credit Agreement. The "Applicable Margin" shall be 0.00% through April 30, 2002 and thereafter shall be 1.00% through October 31, 2002, and thereafter shall be 2.00%.

This Promissory Note is one of the Tax-Exempt Bonds referred to in the Credit Agreement and is secured by the Collateral. "Collateral" shall mean the Interest and Fees Account established pursuant to the Credit Agreement, amounts on deposit in the Interest and Fees Account, securities credited to the Interest and Fees Account, the

Water Code Collateral and all proceeds of the foregoing and all rights of whatever nature associated therewith. "Water Code Collateral" shall mean all Revenues and the right of the State to receive the same, and all moneys on deposit in or credited to the Electric Power Fund (as defined in the Credit Agreement) and the income and revenue derived from the investment thereof and the rights of the State to receive such moneys, income and revenue. "Revenues" shall mean all moneys and amounts payable to or received by or on behalf of the Department for or in connection with the sale of electrical power pursuant to Assembly Bill No. 1 of the First Extraordinary Session as approved by the Governor of the State on February 1, 2001 and filed with the California Secretary of State on February 1, 2001, and as in effect on the date hereof, and from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session and Executive Order D-42-01 of the Governor of the State of California adopted pursuant to the Proclamation of the Governor of the State of California made on January 17, 2001.

The obligations evidenced by this Promissory Note are limited obligations of the Department payable solely from the Revenues and the Collateral described above.

As provided in the Credit Agreement, this Promissory Note is subject to voluntary prepayment without premium or penalty, in whole or in part, upon five (5) Business Days' prior written notice, any partial prepayment to be in an aggregate principal amount of at least $50,000,000 and $5,000,000 multiples in excess thereof applied pro rata among the Loans of all Lenders. As further provided in the Credit Agreement, this Promissory Note is also subject to mandatory prepayment in the event the State or any department, agency or other political subdivision thereof issues any Water Code Bonds (as defined in the Credit Agreement) or incurs or permits to exist any other Debt payable from or secured by the Water Code Collateral, in each case other than Permitted Debt (as defined in the Credit Agreement), and in certain other events, all as more specifically described in the Credit Agreement.

SPECIMEN

The Credit Agreement permits amendment or waiver of the terms thereof by the Department, the Majority Lenders and the Agent; provided, however, that no such change, waiver, discharge or termination shall, without the consent of each Lender, (a) extend any scheduled payment date or the final maturity of any Loan or Bond, or reduce the rate or extend the time of payment of interest or fees thereon, or reduce the principal amount thereof (it being understood that a waiver of any Default, Event of Default, Noncompliance or Event of Noncompliance not declared shall not constitute such an extension, reduction or increase), (b) release any Collateral except as specifically provided in any Transaction Document, (c) amend, modify or waive the amendment provisions or certain other specified provisions of the Credit Agreement, or (d) change the percentage specified in the definition of "Majority Lenders" or "Super Majority Lenders."

The Department hereby waives presentment, demand, protest or notice of any kind in connection with this Promissory Note.

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By:_____
Title: Director, Department of Water Resources

SPECIMEN

THIS PROMISSORY NOTE SHALL BE CONSTRUED IN ACCORDANCE WITH AND BE GOVERNED BY THE LAW OF THE STATE OF CALIFORNIA.

STATE OF CALIFORNIA
Acting through the
DEPARTMENT OF WATER RESOURCES

By: _____
Title: Director, Department of Water Resources

SPECIMEN

Moody's Investors Service

99 Church Street
New York, New York 10007

Chee Mee Hu
Managing Director,
Public Finance Group
Tel: 212.553.3665

Mr. Philip Angelides
Treasurer
State of California

Dear Mr. Angelides:

J. P. Morgan Securities Inc., as the lead arranger and book manager for an interim loan facility for the California Department of Water Resources (CDWR) Electricity Purchase Program, has requested a private credit rating from Moody's Investors Service in conjunction with the interim loan facility. Assembly Bill (AB) 1X, Chapter 4 of the 2001 California State Statutes signed into law on February 1, 2001 requires an investment grade rating as a condition for the interim financing. Moody's understands that the interim loan facility will be refinanced through the issuance of long term bonds some time later this summer or early fall.

To evaluate your request, we have examined information provided to us by parties to the transaction including the CDWR, Navigant, consultant to the CDWR, representatives of the California State Treasurer's Office and the California Department of Finance, J.P. Morgan on behalf of the interim lenders, and various legal consultants to the transaction. We have reviewed various transaction documents including bond counsel opinion confirming the enforceability of the interim financing, the constitutionality of AB 1X and the availability of the State's General Fund balances for liquidity requirements from existing appropriations, as well as an opinion that any future rate increases in accordance with a valid, final and irrevocable CPUC order adopted to meet CDWR's revenue requirements would be deemed the sole property of CDWR. Moody's rating recognizes that bonding authorization for at least $10 billion of long term debt necessary to refinance the interim loan facility and to repay advances to the general fund have been approved by the state legislature. Furthermore the legislature has enacted amendments to AB IX to provide for continuing general fund appropriations and to provide for ongoing liquidity for power purchases until November 15, 2001; after such date, liquidity provided by the General Fund for power purchases will be limited to no more than $500 million in the aggregate. This private credit rating is based on documents provided by the financing team as well as on numerous meetings and conference calls over the past several weeks.

Moody's rating committee has assigned an indicative investment grade rating to the interim loan facility as proposed. Moody's investment grade rating is subject to a number of conditions and assumptions.

- Moody's must be able to confirm that any amendments to AB IX do not negatively affect our rating assessment.
- Prior to the closing of the long term bonds, in addition to the legal opinions provided for the short term interim loan, Moody's must be in receipt of various requisite legal opinions including bond counsel opinion confirming the enforceability of the bonds, and an opinion regarding the servicer agreements or an alternative to the servicer agreements acceptable to Moody's.

Moody's rating is subject to the following assumptions which are key to maintaining the investment grade rating.

- Moody's expects that CDWR will receive the revenues from all CPUC approved rate increases for its power purchases until such time as the bankruptcy judge or State court rules on refunds to PG&E.
- Moody's expects that an acceptable revenue requirement test designed to trigger rate increases necessary to meet CDWR's revenue requirements will be established prior to the issuance of long term bonds. An acceptable rate coverage test will be essential to maintaining the investment grade interim facility credit rating.
- There will not be any material loss of power purchase contracts.

Moody's investment grade rating is based on information provided by the California Department of Water Resources Electricity Purchase Program interim financing team. A material change in the assumptions underlying the rating assignment would warrant a reassessment which could result in a change in the rating. In order for us to maintain the currency of this private rating, we request that you provide ongoing disclosure of relevant credit information. Moody's will monitor this rating and reserves the right, at its sole discretion, to revise or withdraw this rating at any time in the future based on material changes in credit position.

This letter may be used by the California Department of Water Resources Electricity Purchase Program on a confidential basis for the purposes of satisfying credit rating requirements established by AB 1X. Unless directed to do so, Moody's will not publicly disseminate the investment grade rating. However, we reserve the right to express comments regarding the credit issues that are critical to our assessment of the situation at hand.

We hope that this is responsive to your needs. If you have any questions regarding this rating please contact myself or the analyst assigned to this transaction Dan Aschenbach (212-553-0880).

Sincerely,

Chee Mee Hu

June 8, 2001

Ratings Services
55 Water Street, 38th Floor
New York, NY 10041-0003
Tel 212 438-2066
Reference No.: 986543

Steven J. Murphy
Managing Director
Public Finance Ratings

Standard & Poor's
A Division of The McGraw-Hill Companies

REVISED COPY

June 7, 2001

The Honorable Philip Angelides
State Treasurer
State of California
P.O. Box 942809 (94209)
915 Capital Mall – Room 110
Sacramento, CA 95814

Re: ***An Amount up to $6 Billion, State of California, Interim Loan Facility for the California Department Water Resources, dated: Date of Delivery, due: November 1, 2004***

Dear Treasurer Angelides:

Pursuant to your request, Standard & Poor's has performed a credit assessment in connection with the proposed interim loan facility of up to $6 billion to be extended by J.P Morgan, Lehman Brothers, and other banks to the California Department of Water Resources (DWR) (the "Facility").

We have reviewed the information submitted by you and your advisors and, based on the assumptions and the qualifications requested by you, including, without limitation, the qualifications listed below, Standard & Poor's credit assessment opinion is that the Facility has a credit profile consistent with obligations rated by Standard & Poor's in the 'BBB' category.

You understand and agree that a credit assessment is a credit opinion based solely on the facts and circumstances presented to us by you and your advisors and (i) the credit assessment is being provided solely for your use in estimating the credit quality of the Facility (ii) additional information or changes to the information previously presented to us may result in credit risk higher or lower than the credit assessment might suggest, (iii) the credit assessment is an opinion on the estimated creditworthiness of the Facility -- actual credit qualities may be higher or lower than those determined by the credit assessment and the credit assessment is not a prediction of the actual performance of the Facility in the future, (iv) we do not and cannot warrant suitability of the credit assessment for any particular purpose or use, (v) the credit assessment is provided without any express or implied warranties whatsoever, (vi) the credit assessment is based on information solely supplied to us by you and does not represent an audit of the Facility or the Department, (vii) we rely on you, your accountants, counsel and other experts for the accuracy and completeness of the information submitted in connection with the credit assessment (viii) in providing the credit assessment we do not, and will not undertake to provide a rating of the credit risk of the Facility and the credit assessment shall not be construed to have been undertaken with the rigor and level of detail required for Standard & Poor's to provide a rating opinion, and (ix) we do not and cannot guarantee the accuracy, completeness or timeliness of the information relied on in connection with the credit assessment, or the results obtained from the use of such information. Please note that the credit assessment speaks only as of the date hereof and is not subject to surveillance or update.

Without limiting any of the statements made in the previous paragraph, we set forth below some of the factors considered in the analysis, which, in our opinion, have a material effect on the credit assessment and may significantly affect our ability to issue the rating on any refinancing in the future:

1. The Facility will be refinanced by the DWR in late 2001 through a capital markets bond issuance and, accordingly, the credit assessment is premised on the occurrence of such refinancing and the terms and conditions thereof.

2. The terms of the refinancing bonds will include a "rate covenant" requiring the DWR to determine a Revenue Requirement sufficient to provide annual net revenues, after the payment of DWR power procurement and operating expenses, equivalent to at least 1.35 times the DWR's annual debt service obligations under the refinancing bonds. The Revenue Requirement will be submitted to the California Public Utilities Commission (CPUC), which is responsible for imposition of retail electric charges sufficient for the DWR to satisfy the Revenue Requirement. Additionally, the DWR will enter into a Rate Agreement with the CPUC establishing the mechanism for implementing the rate covenant to ensure timely payment of scheduled debt service on the refinancing bonds. The DWR will have received legal opinions satisfactory in form and substance concluding that such Rate Agreement is valid, enforceable (against both the DWR and the CPUC) and constitutional, as well as legal opinions, satisfactory in form and substance, concluding that any CPUC order implementing the rate covenant is valid, enforceable and constitutional.

3. The DWR will have received a legal opinion satisfactory in form and substance concluding that the revenues from which debt service payments on the refinancing bonds are derived have been pledged to the indenture trustee or collateral agent for the refinancing bonds.

4. The DWR will have received a legal opinion satisfactory in form and substance concluding that a bankruptcy filing by any of the State's investor owned utilities will not interrupt or otherwise adversely affect the payment to the DWR by the utilities of revenues pledged to debt service on the refinancing.

5. The relevant documentation for the refinancing (including, without limitation, purchase power contracts entered into by the DWR) are consistent with Standard & Poor's criteria for low investment grade ratings.

For the avoidance of doubt, the failure by the CPUC to raise rates as and when needed to ensure timely payment of debt service on the refinancing bonds may result in rating action taken against the State of California.

This credit assessment is provided to you for your sole use. You may reveal the credit assessment confidentially to your financial advisors or other entities that are party to the proposed Facility in connection with your business dealings and negotiations of the Facility only by delivering to each party a copy of this entire letter containing the limitations of the credit assessment. However, you may not disseminate the credit assessment to potential third party investors. Standard and Poor's reserves the right to release this credit assessment letter for public dissemination in the event the credit assessment is publicly disclosed.

You understand that Standard & Poor's has not consented to, and will not consent to, being named an 'expert" under the federal securities laws, including without limitation, Section 7 of the Securities Act of 1933. In addition, it should be understood that the rating is neither a "market" rating nor a recommendation to buy, hold, or sell the instruments. Standard & Poor's reserves the right to advise its own clients, subscribers, and the public of the rating.

We are pleased to have had the opportunity of being of service to you. If we can be of any further help, please do not hesitate to call upon us.

Very truly yours,

ed

cc: Mr. Nathan Brostrom, Vice President
J. P. Morgan Securities Inc.

FITCH

FITCH IBCA, DUFF & PHELPS

June 12, 2001

Hon. Philip Angelides
State Treasurer
State of California
915 Capitol Mall; Room 280
Sacramento, California 95814

Dear Mr. Angelides:

You have requested that Fitch review a proposed Interim Loan Facility of the California Department of Water Resources and express an opinion regarding its credit worthiness. We understand that the loan amount will be not more than $6.0 billion and that it will be secured by a pledge of proceeds of bonds to be issued and net revenues of the borrower-the Department of Water Resources. The basis of our analysis is the June 11, 2001 draft of the Credit and Security Agreement. The Credit and Security Agreement authorization would be based on Division 27 of the California Water Code and an Emergency Order of the Governor which would be issued under the Emergency Services Act. We have also reviewed draft validity opinions and bankruptcy opinions, and assume there will be no substantive changes. The validity opinions reviewed include Orrick, Herrington & Sutcliffe LL.P drafts from 5/28/01. The bankruptcy opinions reviewed include Hawkins Delafield & Wood drafts dated 5/7/01 and Orrick Herrington & Sutcliffe drafts dated 5/4/01 relating to the Electrical Corporations. It is assumed that prior to closing of the loan, we will review the final agreement as well as updates of other pertinent information related to the transaction and the Department of Water Resources power purchase program.

Loan repayment effectively requires the issuing of Power Supply Bonds by the Department of Water Resources and the Fitch assessment factors in the likelihood of such issuance. We assume, as do the bankruptcy opinions, the condition that a CPUC rate agreement or rate order will be in full force and effect prior to the issuance of the Power Supply Bonds and that a servicing agreement with the Electrical Corporations or a CPUC servicing order will also be in full force and effect prior to the issuance of the Power Supply Bonds.

It is also assumed that prior to closing of the interim loan facility appropriate final legal opinions will be submitted to Fitch for review including, among others, the validity and enforceability of the Emergency Order and the loan and its security. Based on the foregoing, Fitch believes that the interim loan facility to be of investment grade quality.

Sincerely,

Richard J. Raphael
Executive Managing Director

RJR:ld
cc: Lai Louie --- State of California Treasurer's Office

$2,000,000,000
CALIFORNIA DEPARTMENT OF WATER RESOURCES
INTERIM ENERGY FINANCING BRIDGE LOAN
TAX-EXEMPT BONDS AND TAX-EXEMPT LOANS

TAX CERTIFICATE

The State of California, acting through its Department of Water Resources (the "Department"), hereby makes the following representations of facts and expectations and covenants to comply with the requirements of this Tax Certificate in connection with the Department's Interim Energy Financing Bridge Loan, Tax-Exempt Bonds and the Tax-Exempt Loans evidenced thereby made pursuant to the Credit Agreement (as defined below), in the aggregate principal amount of $2,000,000,000 (collectively, the "Tax-Exempt Obligations"). These representations and covenants are in furtherance of the covenants contained in Section 6.14 of the Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement"), by and among the State of California (the "State") acting through the Department, various lenders (collectively, the "Lenders"), and Morgan Guaranty Trust Company of New York, as agent (the "Agent"), and in part are made pursuant to Section 1.148-2(b)(2) of the Treasury Regulations. Capitalized terms used herein which are not otherwise defined herein shall have the respective meanings set forth in the Credit Agreement.

1. GENERAL MATTERS.

1.1 Authorization for Execution and Delivery. The undersigned is charged with the responsibility of authorizing and requesting the execution and delivery of the Tax-Exempt Obligations. The Tax-Exempt Obligations are being executed and delivered pursuant to the Constitution and laws of the State of California (the "State"), including Assembly Bill No. 1 of the First Extraordinary Session as approved by the State Governor on February 1, 2001 and filed with the State Secretary of State on February 1, 2001, and as in effect on the date hereof and, from and after August 15, 2001, as amended by Senate Bill No. 31 of the First Extraordinary Session as approved by the State Governor on May 10, 2001 and filed with the California Secretary of State on May 10, 2001, as in effect on the date hereof (collectively, "AB1X"), a Proclamation of the State Governor dated January 17, 2001 concerning the state of emergency due to shortages of electricity available in the State (the "Emergency Proclamation") issued pursuant to the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code (the "Emergency Services Act")), Executive Order D-42-01 signed by the State Governor on June 18, 2001 (the "Order") to effectuate the purposes of the Emergency Services Act and the clarify and effectuate features of the Emergency Proclamation, and Division 27 (commencing with Section 80000) of the California Water Code, as amended by Statutes 2001, Chapter 4 and thereafter ("Division 27"), as well as the Credit Agreement.

AB1X, the Emergency Proclamation, the Emergency Services Act and the Order authorize the Department to purchase electric power; to enter into short-term and long-term contracts for the purchase of electric power, and to sell such electric power to its retail end-use customers in the State. Further the Department is authorized to enter into short-term long-term loans, including accepting an offer to purchase bonds, notes and other obligations to finance its purchase of electric power or to refund such loans, or to reimburse the General Fund of the State for amounts expended

for such purchases, and to impose charges and collect revenue sufficient to fund such electric power purchases (including the payment of debt service on obligations issued by the Department to fund such power purchases). In addition, AB1X, the Emergency Proclamation, the Emergency Services Act and the Order provide that in order to effectuate the purchase and sale of electric power by the Department, "electrical corporations" (as defined in Section 218 of the California Public Utilities Code), acting as the Department's agent, shall provide transmission, metering, billing, collection and other related services to the Department for all the power made available by the Department. Any amounts that have been or will be advanced to the Department by the State from its General Fund are required to be replenished thereby as soon as possible and without condition and, except for those amounts that have been or will be actually advanced to the Department for such purpose pursuant to prior legislative authorization, moneys in the General Fund are not otherwise available to be used by or on behalf of the Department for the satisfaction of its obligations incurred in connection with the purchase of its electric power (including indebtedness issued therefor).

1.2 Delivery and Sale of Tax-Exempt Obligations. The Tax-Exempt Obligations are being sold and delivered to the Lenders on the date hereof in exchange for good funds. The transaction was arranged by JPMorgan Securities Inc., as Lead Arranger and book manager (the "Lead Arranger"). The Tax-Exempt Obligations will not be resold to the general public. The Tax-Exempt Obligations are being purchased in a direct, private placement transaction and the terms of the sale and purchase have been established through negotiations between the Lenders and the Department in an arm's-length transaction. The purchase price payable by the Lenders will be 100% of the aggregate principal amount of the Tax-Exempt Obligations. Montague, DeRose & Associates has provided certain financial advice to the Department with respect to this financing.

1.3 Purpose of Tax-Exempt Obligations. The Tax-Exempt Obligations are being made for the purpose of (a) financing on an interim basis a portion of the cost of electric power made by the Department for its retail end-use customers in the State pursuant to arrangements having a term (including, if applicable, renewal options) of one year or less (the "Project"), (b) to pay a portion of the interest accruing with respect to the Tax-Exempt Obligations prior to the Term Out Period Commencement Date ("Capitalized Interest"), and (c) costs incurred by the Department in connection with the execution and delivery of the Tax-Exempt Obligations, including an allocable share of such costs which are common to both the Tax-Exempt Obligations and the Taxable Obligations (referred to below). The Department covenants to use the proceeds of the Tax-Exempt Obligations solely for the above-described purposes, unless an opinion of Bond Counsel is received to the effect that uses of proceeds for other than the above-described purposes will not adversely affect the exclusion from gross income of interest on the Tax-Exempt Obligations.

1.4 Nature of Issue. The Tax-Exempt Obligations are a single issue of obligations for certain federal income tax purposes relating to the exclusion from gross income of interest with respect to the Tax-Exempt Obligations. Except as provided below, no other governmental obligations which are reasonably expected to be paid from substantially the same source of funds are being sold at substantially the same time and sold pursuant to the same plan of financing as the Tax-Exempt Obligations.

1.4.1 Taxable Obligations. Concurrently with the execution and delivery of the Tax-Exempt Obligations, the Department is causing the execution and delivery pursuant to the Credit Agreement of $2,300,000,000 aggregate principal amount of Taxable Bonds and Taxable Loans evidenced thereby (collectively, the "Taxable Obligations"), the interest on which is not excluded

from gross income for federal income tax purposes. The Department is using proceeds of the Taxable Obligations to finance other purchases of electric power. Pursuant to Section 1.150-1(c)(2) of the Treasury Regulations, however, the Tax-Exempt Obligations and the Taxable Obligations are not part of the same "issue" for federal income tax purposes. Further, the Department is not executing and delivering the Taxable Obligations as part of a transaction that employs an "abusive arbitrage device" under Section 1.148-10(a) or a device to avoid other limitations in Sections 103 and 141 through 150 of the Code.

1.5 Purpose of Tax Certificate. The Department is executing this Tax Certificate with the understanding and acknowledgement that Hawkins, Delafield & Wood ("Bond Counsel") will rely on the representations and certifications made in this Tax Certificate (including all exhibits hereto) in rendering its opinion that interest with respect to the Tax-Exempt Obligations are excluded from gross income for federal income tax purposes, and the execution of this Tax Certificate is necessary to ensure that interest with respect to the Tax-Exempt Obligations are excluded from gross income for federal income tax purposes.

2. PRIVATE ACTIVITY.

2.1 Governmental Use of Proceeds. The Department has sold electric power to its retail end use customers pursuant to tariffs established by the Department or approved by the California Public Utilities Commission (the "CPUC") and will contract with, or ask the CPUC to order, electrical corporations (as defined in Section 218 of the California Public Utilities Code) to provide transmission, distribution, billing and collection services in connection therewith, all in accordance with the Act, the Emergency Proclamation, the Order and Division 27 of the California Water Code. The Department will not allow any of the proceeds of the Tax-Exempt Obligations to be used in the trade or business of any nongovernmental persons (other than in their roles as members of the general public) and will not loan any of the proceeds of the Tax-Exempt Obligations to any nongovernmental persons.

2.2 In General. None of the proceeds of the Tax-Exempt Obligations or the Project has been or will be used for any activities that constitute a "Private Use" (as such term is defined in Section 2.5 hereof). None of the principal of or interest with respect to the Tax-Exempt Obligations, under the terms thereof or any underlying arrangement, has been or will be secured by any interest in property used for a Private Use or in payments in respect of property used for a Private Use, or will be derived from payments in respect of property used for a Private Use.

2.3 No Private Loan Financing. None of the proceeds of the Tax-Exempt Obligations will be used to make or finance loans to any person other than to a state or local governmental unit (other than loans to finance any governmental tax or assessment of general application for a specific essential governmental function or loans that are used to acquire or carry Nonpurpose Investments (as such term is defined in Exhibit D attached hereto)).

2.4 No Disproportionate or Unrelated Use. None of the proceeds of the Tax-Exempt Obligations or the Project has been or will be used for a Private Use that is unrelated or disproportionate to the governmental use of the proceeds of the Tax-Exempt Obligations (an "Unrelated or Disproportionate Use"), and none of the principal of or interest with respect to any of the Tax-Exempt Obligations have been or will be, under the terms of the Tax-Exempt Obligations or any underlying arrangement, directly or indirectly, secured by any interest in property used or to be

used for a Private Use that is an Unrelated or Disproportionate Use or in payments in respect of property used or to be used for a Private Use that is an Unrelated or Disproportionate Use.

2.5 Definition of Private Use. For purposes of this Tax Certificate, the term "Private Use" means any activity that constitutes a trade or business that is carried on by persons or entities, other than governmental entities. The leasing of property financed or refinanced with proceeds of the Tax-Exempt Obligations or use by or the access of a person or entity other than a governmental entity to property or services on a basis other than as a member of the general public shall constitute a Private Use. For this purpose, "governmental entity" means a State or any political subdivision thereof (as defined in Section 1.103-1 of the Treasury Regulations).

2.6 Management and Service Contracts. As of the date hereof, no portion of the proceeds derived from the sale of the Tax-Exempt Obligations are being used to provide property subject to contracts or other arrangements with persons or entities engaged in a trade or business (other than governmental entities) that involve the management of property or the provision of services with respect to property financed by proceeds of the Tax-Exempt Obligations.

3. ARBITRAGE CERTIFICATIONS.

The following states the expectations of the Department with respect to the amount and uses of the proceeds of the Tax-Exempt Obligations and certain other moneys or property:

3.1 Source and Use of Funds. The Department will deliver the Tax-Exempt Obligations on the date hereof to the Lenders. The purchase price of the Tax-Exempt Obligations is equal to $2,000,000,000.00 (being the aggregate stated principal amount of the Tax-Exempt Obligations). These proceeds are expected to be needed and fully expended as follows:

3.1.1 $1,909,055 ,000.00 of said proceeds will be deposited on the date hereof in the Electric Power Fund and are expected to be used, together with anticipated earnings thereon, within six months (and in all events, within thirteen months) of the date hereof to pay the costs of the Project;

3.1.2 $31,781,750.00 of said proceeds will be deposited in the Interest and Fees Account on the date hereof and used to pay on or before October 31, 2001 a portion of the interest accruing on or before such date with respect to the Tax-Exempt Obligations; and

3.1.3 $59,163,250.00 of said proceeds will be deposited in the Interest and Fees Account on the date hereof and used as follows: $2,850,000.00 of which shall be used on or before October 31, 2001 (and in all events, within thirteen months) to pay costs incurred by the Department in connection with the execution and delivery of the Tax-Exempt Obligations, and $56,313,250.00 of which shall be used to pay additional interest on the Tax-Exempt Obligations during the period after October 31, 2001 or additional costs of the Project.

3.2 No Reimbursement. No portion of the proceeds of the Tax-Exempt Obligations will be used to reimburse the Department for expenditures incurred and paid in connection with the Project prior to the execution and delivery of the Tax-Exempt Obligations.

3.3 Overissuance. The total proceeds received by the Department from the execution and delivery of the Tax-Exempt Obligations, together with anticipated investment earnings thereon, do not exceed the total amount necessary for the governmental purposes described above.

3.4 Temporary Period. The Department reasonably expects that the proceeds derived from the sale of the Tax-Exempt Obligations will be allocated to expenditures for the Project within thirteen months of the date hereof.

3.5 Funds and Accounts. The Credit Agreement creates and establishes the following funds and accounts with respect to the Tax-Exempt Obligations:

3.5.1 the Interest and Fees Account.

In addition, the "Department of Water Resources Electric Power Fund" (the "Electric Power Fund") was created by Section 80200 of the Water Code.

3.6 Sinking Funds.

3.6.1 Payment of Debt Service. The portion of Revenues deposited to the Electric Power Fund that will be used to pay debt service on the Tax-Exempt Obligations (the "Sinking Fund Portion of the Electric Power Fund") and the moneys deposited to the Interest and Fees Account (collectively, the "Bona Fide Debt Service Funds") will be used primarily to achieve a proper matching of revenues (and certain other moneys) and payments of principal and interest with respect to the Tax-Exempt Obligations within each year. Amounts deposited in the Bona Fide Debt Service Funds will be depleted at least once each Bond Year except for a reasonable carryover amount, if any, which, in the aggregate, will not exceed the greater of (i) one year's earnings on such funds for the immediately preceding Bond Year, or (ii) one-twelfth of the annual debt service on the Tax-Exempt Obligations for the immediately preceding Bond Year.

3.6.2 Reserve Amount. No reserve or replacement fund will be created or established in connection with the execution and delivery of the Tax-Exempt Obligations.

3.6.3 No Negative Pledges. There are no amounts held under any agreement to maintain amounts at a particular level for the direct or indirect benefit of the holders of the Tax-Exempt Obligations or guarantor of the Tax-Exempt Obligations, if any, excluding for this purpose amounts in which the Department (or a substantial beneficiary) may grant rights that are superior to the rights of the holders of the Tax-Exempt Obligations or guarantor of the Tax-Exempt Obligations, if any, and amounts that do not exceed reasonable needs for which they are maintained and as to which the required level is tested no more frequently than every six (6) months and that may be spent without any substantial restriction other than a requirement to replenish the amount by the next testing date.

3.7 Electric Power Fund. The Electric Power Fund was established pursuant to Section 80200 of the Water Code. Moneys held therein will be used as provided in Section 6.7 of the Credit Agreement; in particular, moneys in the Electric Power Fund shall only be expended to pay Operating and Maintenance Costs (which include satisfaction of any Power Obligations (as such term is defined in the Credit Agreement) of the Department), the principal of and interest with respect to the Tax-Exempt Obligations and the Taxable Obligations and Permitted Debt, all other amounts

payable under the Credit Agreement and the other Transaction Documents, and any other amounts required by law to be paid from the Electric Revenue Fund.

3.8 No Other Proceeds. Other than the Electric Power Fund and the Interest and Fees Account, there are no funds or accounts of the Department established pursuant to the Credit Agreement, the Transaction Documents, or otherwise, that are reasonably expected to be used for the payment of principal and interest with respect to the Tax-Exempt Obligations or that are pledged as collateral for the Tax-Exempt Obligations and for which there is a reasonable assurance that amounts on deposit therein will be available for the payment of principal and interest with respect to the Tax-Exempt Obligations if the Department encounters financial difficulties.

3.9 No Rebate Fund. No rebate fund was established with respect to the Tax-Exempt Obligations.

3.10 No Replacement Proceeds. The term of the Tax-Exempt Obligations are not longer than is reasonably necessary for the governmental purpose of the issue, and the weighted average maturity of the Tax-Exempt Obligations does not exceed 2 years.

3.11 Arbitrage Investment Restrictions. The proceeds derived from the sale of the Tax-Exempt Obligations and the amounts on deposit in the aforementioned funds and accounts may be invested as follows:

3.11.1 Accrued Interest. No amounts were derived from the sale of the Tax-Exempt Obligations to pay pre-issuance accrued interest with respect to the Tax-Exempt Obligations.

3.11.2 Issuance Costs. Proceeds derived from the sale of the Tax-Exempt Obligations deposited to the Interest and Fees Account used to pay costs and fees incurred with respect to the execution and delivery of the Tax-Exempt Obligations may be invested at an unrestricted yield for a period not to exceed thirteen months from the date of deposit of such amounts to such Account.

3.11.3 Project Costs. Proceeds derived from the sale of the Tax-Exempt Obligations that are deposited in the Electric Power Fund to finance the cost of the Project may be invested at an unrestricted yield for a period not to exceed thirteen months from the date hereof and, thereafter, shall be invested at a yield not in excess of the yield with respect to the Tax-Exempt Obligations plus one-eighth of one percentage point (1/8%). Investment earnings on obligations acquired with such proceeds may be invested at an unrestricted yield for a period not exceeding one year from the receipt thereof and, thereafter, shall be invested at a yield not in excess of the yield with respect to the Tax-Exempt Obligations plus one-eighth of one percentage point (1/8%).

3.11.4 Payment of Debt Service. Amounts deposited in the Bona Fide Debt Service Funds (other than as pre-issuance accrued interest, if any) may be invested at an unrestricted yield for a period not to exceed thirteen months from the date of deposit of such amounts to such fund. Earnings on such amounts that are retained in such fund may be invested at an unrestricted yield for a period not to exceed one year from the date of receipt of the amount earned.

3.11.5 Minor Portion. Amounts described in this Section 3.11 that may not be invested at an unrestricted yield as described above may be invested at an unrestricted yield to the

extent such amounts do not exceed the lesser of five percent (5%) of the sale proceeds of the Tax-Exempt Obligations or $100,000 (the "Minor Portion").

3.11.6 Yield Restricted Moneys. Proceeds derived from the sale of the Tax-Exempt Obligations and investment earnings thereon that may not be invested at an unrestricted yield pursuant to this Section 3.11 will either (i) be invested at a yield not in excess of the yield with respect to the Tax-Exempt Obligations (or, where applicable, at a yield not in excess of the yield with respect to the Tax-Exempt Obligations plus one-eighth of one percentage point), or (ii) be invested in Tax-Exempt Investments (as hereinafter defined in Exhibit D hereto). Gross Proceeds (as such term is defined in Exhibit D hereto) and investment earnings thereof that may not be invested at an unrestricted yield pursuant to this Section 3.11 will either (i) be invested at a yield not in excess of the yield with respect to the Tax-Exempt Obligations, or (ii) be invested in Tax-Exempt Investments.

3.12 Yield. Since the Tax-Exempt Obligations are being initially executed and delivered in a variable rate mode, the yield with respect to the Tax-Exempt Obligations cannot be determined as of the date hereof. The Department shall seek expert advice in determining the yield with respect to the Tax-Exempt Obligations. For purposes of this Tax Certificate, yield is calculated as set forth in Section 148 of the Code, and Section 1.148-4 of the Treasury Regulations. Thus, yield generally means that discount rate which when used in computing the present value as of the first day of a computation period (the "Computation Period") of all unconditionally payable payments representing principal, interest, and the cost of qualified guarantees paid and to be paid with respect to the applicable obligations attributable to the Computation Period produces an amount equal to the issue price of the applicable obligations (or deemed issue price) as of the first day of the Computation Period. Yield with respect to the obligations allocable to proceeds of the Tax-Exempt Obligations is that discount rate which when used in computing the present worth of the payments of principal and interest with respect to the obligations produces an amount equal to the purchase price of the obligation.

3.12.1 Computation Period. For purposes of this Tax Certificate, a Computation Period begins on the delivery date of the Tax-Exempt Obligations and ends on the date selected by the Department in accordance with Treasury Regulation §1.148-3(e), which in no event is later than the date preceding the fifth anniversary from the delivery date, and each succeeding five-year (or shorter) period thereafter (as provided in Treasury Regulation §1.148-3(e)) until there are no longer any Tax-Exempt Obligations outstanding.

3.12.2 No Qualified Guarantee Fee. No amount has been or will be paid by or on behalf of the Department to any entity as a payment for a "qualified guarantee" (as such term is defined in Section 1.148-4(f) of the Treasury Regulations).

3.12.3 Special Rule for Optional Early Redemption. None of the Tax-Exempt Obligations (i) is being executed and delivered at an issue price that exceeds the stated redemption price at maturity by more than one-fourth of one percent (.25%) multiplied by the product of the stated redemption price at maturity and the number of complete years to the first optional redemption date for the bond, or (ii) bears interest at increasing interest rates (*i.e.*, a stepped coupon bond). Pursuant to the Credit Agreement, the Tax-Exempt Obligations are subject to repayment on any date at the option of the Department, in accordance with Section 3.2 of the Credit Agreement.

3.12.4 Special Rule for Term Bonds. None of the Tax-Exempt Obligations consist of term bonds that require mandatory sinking fund payments on dates prior to their stated maturity date.

3.12.5 Investment Contract. The Department has not invested any proceeds of the Tax-Exempt Obligations pursuant to an investment contract (within the meaning of Section 1.148-1(b) of the Treasury Regulations).

3.13 Yield Reduction Payments. Notwithstanding the provisions of Section 3.11 above that require the Department to invest proceeds derived from the sale of the Tax-Exempt Obligations and investment earnings thereon at a yield not in excess of the yield with respect to the Tax-Exempt Obligations, the yield on certain nonpurpose investments acquired with proceeds of the Tax-Exempt Obligations will not be considered to be higher than the applicable yield limitation described in Section 3.11 above if the Department makes or causes to be made "yield reduction payments" to the United States Treasury at the time and in the amounts described in Section 1.148-5(c) of the Treasury Regulations.

3.14 No Artifice or Device. The Tax-Exempt Obligations are not and will not be part of a transaction or series of transactions (i) that attempts to circumvent the provisions of Section 148 of the Code, or any successor thereto, and the regulations promulgated thereunder or under any predecessor thereto, enabling the Department or any related person to exploit the difference between tax-exempt and taxable interest rates to gain a material financial advantage, and (ii) that increases the burden on the market for the obligations in any manner, including, without limitation, by selling bonds that would not otherwise be sold, or selling more bonds, or issuing bonds sooner, or allowing bonds to remain outstanding longer, than otherwise would be necessary.

4. MISCELLANEOUS.

4.1 Federal Guarantee. The Department will not invest any of the proceeds of the Tax-Exempt Obligations in a manner which would result in the Tax-Exempt Obligations being considered "federally guaranteed" within the meaning of Section 149(b) of the Code, except as permitted therein.

4.2 Information Reporting. Attached as Exhibit B is a copy of the Form 8038-G with respect to the Tax-Exempt Obligations. The Department will file or cause to be filed such reports or other documents with the Internal Revenue Service as is required by the Code.

4.3 No Pooling. The Department does not expect to use and will not use the proceeds of the Tax-Exempt Obligations to make or finance loans to two or more ultimate borrowers.

4.4 Hedge Bonds. The proceeds derived from the sale of the Tax-Exempt Obligations are reasonably expected to be expended within thirteen months of the date hereof. Additionally, no more than fifty percent (50%) of the net sale proceeds of the Tax-Exempt Obligations will be invested in Nonpurpose Investments at a substantially guaranteed yield for four years or more. Therefore, the Tax-Exempt Obligations satisfy the requirements of Section 149(g) of the Code.

4.5 Qualified Hedging Transaction. The Department has not engaged, and will not engage, in any qualified hedging transaction (as such term is defined in Section 1.148-4(h)(2) of the Treasury Regulations) with respect to the Tax-Exempt Obligations.

5. CONCLUDING MATTERS.

5.1 Reliance. The expectations of the Department concerning certain uses of proceeds derived from the sale of the Tax-Exempt Obligations and certain other moneys described herein and other matters are based in whole or in part upon representations of the Lead Arranger and other parties set forth in this Tax Certificate and in the exhibits hereto. The Department is not aware of any facts or circumstances that would cause it to question the accuracy or reasonableness of any representation made in this Tax Certificate or in the exhibits hereto, including those representations made by the Lead Arranger.

5.2 Authorization. The undersigned is an authorized representative of the Department, and is acting for and on behalf of the Department in executing this Tax Certificate. To the best of the knowledge and belief of the undersigned, there are no other facts, estimates or circumstances that would materially change the expectations as set forth herein, and said expectations are reasonable.

5.3 Amendment. Notwithstanding any provision of this Tax Certificate, the Department may amend this Tax Certificate and thereby alter any actions allowed or required by this Tax Certificate if such amendment is based on an opinion of nationally-recognized bond counsel that the exclusion from gross income of interest with respect to the Tax-Exempt Obligations will not be adversely affected.

Dated: June 26, 2001

THE STATE OF CALIFORNIA
acting through the
DEPARTMENT OF WATER RESOURCES

By: Perla Netto-Brown

Perla Netto-Brown
Chief, Fiscal Services Division

EXHIBIT A

$2,000,000,000
CALIFORNIA DEPARTMENT OF WATER RESOURCES
INTERIM ENERGY FINANCING BRIDGE LOAN
TAX-EXEMPT BONDS AND TAX-EXEMPT LOANS

CERTIFICATE OF THE LEAD ARRANGER

This Certificate is furnished by JPMorgan Securities Inc., as the Lead Arranger and book manager (the "Lead Arranger") of the California Department of Water Resources, Interim Energy Financing Bridge Loan, Tax-Exempt Bonds and the Tax-Exempt Loans evidenced thereby made pursuant to a certain Credit and Security Agreement, dated as of June 26, 2001, in the aggregate principal amount of $2,000,000,000 (collectively, the "Tax-Exempt Obligations"), and hereby certifies and represents the following, under penalties of perjury, based upon the information available to it:

1. Issue Price.

1.1 As of June 26, 2001, the date of execution and delivery of the Tax-Exempt Obligations (the "Sale Date"), the issue price of such Tax-Exempt Obligations was not greater than the fair market price of the Tax-Exempt Obligations.

1.2 The Tax-Exempt Obligations are being purchased in a direct, private placement transaction and the terms of the sale and purchase have been established through negotiations between the Lenders and the Department in an arm's-length transaction.

1.3 The purchase price for the Tax-Exempt Obligations to be paid as established through the negotiated transaction described above is an amount equal to 100% of the aggregate principal amount of the Tax-Exempt Obligations.

1.4 The Lead Arranger is arranging the placement of the Tax-Exempt Obligations with the Lenders for their own accounts and will receive a fee in connection with such purchase in the approximate amount of $1,250,000, and expenses of $150,000. In addition, except for the Lead Arranger, each Lender with respect to the Tax-Exempt Obligations is receiving on the date hereof fees in the aggregate equal to $1,250,000 (each such Lender's Commitment multiplied by 0.00125) and $200,000 in administrative fees.

1.5 As of the date hereof, the Lenders have no plans or expectations to sell or transfer the Tax-Exempt Obligations (or any interest therein) to any bond houses, brokers, dealers, wholesalers or similar persons acting in such capacity.

2. Tax Certificate.

We have read the attached Tax Certificate, including all exhibits thereto. Nothing has come to our attention that is inconsistent with the expectations, statements, conditions and covenants stated therein. We confirm all expectations, statements, conditions and covenants in such Tax-Exempt Obligations that are stated to be based upon the representation(s) or advice of the Lead Arranger.

All terms not defined herein have the meanings ascribed to those terms in the attached Tax Certificate.

Dated: June 26, 2001

JPMorgan Securities Inc.

By: _____
Nathan Brostrom
Vice President

SCHEDULE A

Price of Tax-Exempt Obligations

Maturity Date	Maturity Amount	Coupon Rate
10/31/2004	$2,000,000,000	VR

EXHIBIT B

INFORMATION REPORTING

FORM 8038-G

(attached hereto)

Form **8038-G**

(Rev. November 2000)

Department of the Treasury
Internal Revenue Service

Information Return for Tax-Exempt Governmental Obligations

Under Internal Revenue Code section 149(e)

See separate Instructions.

Caution: *If the issue price is under $100,000, use Form 8038-GC.*

OMB No. 1545-0720

Part I Reporting Authority

If Amended Return, check here ☐

1	Issuer's name California Department of Water Resources	2. Issuer's employer identification number 52-1692634	
3	Number and street (or P.O. box if mail is not delivered to street address) 1416 9th Street	Room/suite 805-1	4 Report number 3 2001-2
5	City, town, or post office, state, and ZIP code Sacramento, California 95814		6 Date of issue June 26, 2001
7	Name of issue Interim Emergency Financing Bridge Loan (Tax-Exempt)		8 CUSIP number N/A
9	Name and title of officer or legal representative whom the IRS may call for more information Perla Netto-Brown, Chief, Fiscal Services Office	10 Telephone number of officer or legal representative (916) 653-9836	

Part II Type of Issue (check applicable box(es) and enter the issue price) See instructions and attach schedule

11	☐ Education	11	N/A
12	☐ Health and hospital	12	N/A
13	☐ Transportation	13	N/A
14	☐ Public safety	14	N/A
15	☐ Environment (including sewage bonds)	15	N/A
16	☐ Housing	16	N/A
17	☐ Utilities	17	N/A
18	☒ Other. Describe short-term purchases of electric energy	18	2,000,000,000.00
19	If obligations are TANs or RANs, check box ☐ If obligations are BANS, check box ☒		
20	If obligations are in the form of a lease or installment sale, check box ☐		

Part III Description of Obligations. (Complete for the entire issue for which this form is being filed.)

	(a) Final maturity date	(b) Issue price	(c) Stated redemption price at maturity	(d) Weighted average maturity	(e) Yield
21	10/31/2004	$ 2,000,000,000.00	$ 2,000,000,000.00	.34 years	VR %

Part IV Uses of Proceeds of Bond Issue (including underwriters' discount)

22	Proceeds used for accrued interest			22	0.00
23	Issue price of entire issue (enter amount from line 21, column (b))			23	2,000,000,000.00
24	Proceeds used for bond issuance costs (including underwriters' discount)	24	2,850,750.00		
25	Proceeds used for credit enhancement	25	0.00		
26	Proceeds allocated to reasonably required reserve or replacement fund	26	0.00		
27	Proceeds used to currently refund prior issues	27	0.00		
28	Proceeds used to advance refund prior issues	28	0.00		
29	Total (add lines 24 through 28)			29	2,850,750.00
30	Nonrefunding proceeds of the issue (subtract line 29 from line 23 and enter amount here)			30	1,997,149,250.00

Part V Description of Refunded Bonds (Complete part only for refunding bonds.)

31	Enter the remaining weighted average maturity of the bonds to be currently refunded	years
32	Enter the remaining weighted average maturity of the bonds to be advance refunded	years
33	Enter the last date on which the refunded bonds will be called	
34	Enter the date(s) the refunded bonds were issued	

Part VI Miscellaneous

35	Enter the amount of the state volume cap allocated to the issue under section 141(b)(5)	35	N/A
36a	Enter the amount of gross proceeds invested or to be invested in a guaranteed investment contract (see instructions)	36a	N/A
b	Enter the final maturity date of the guaranteed investment contract		
37	Pooled financings: a Proceeds of this issue that are to be used to make loans to other governmental units	37a	N/A
b	If this issue is a loan made from the proceeds of another tax-exempt issue, check box ☐ and enter the name of the issuer _____ and the date of the issue _____		
38	If the issuer has designated the issue under section 265(b)(3)(B)(i)(III) (small issuer exception), check box ☐		
39	If the issuer has elected to pay a penalty in lieu of arbitrage rebate, check box ☐		
40	If the issuer has identified a hedge, check box ☐		

Sign Here

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete.

Theresa Lightle — June 26, 2001

Signature of issuer's authorized representative — Date

Theresa Lightle
Deputy Comptroller

Type or print name and title

EXHIBIT C

OFFICIAL ACTION

(attach copy)

DECLARATION OF OFFICIAL INTENT OF THE
DEPARTMENT OF WATER RESOURCES OF THE STATE OF
CALIFORNIA REGARDING ITS INTENTION TO ISSUE
TAX-EXEMPT OBLIGATIONS

The undersigned, Thomas Hannigan, Director of the Department of Water Resources of the State of California (the "Department"), as of the date set forth below, does hereby declare as follows:

1. The Department desires to finance the costs of purchasing electrical energy and power made thereby pursuant to Assembly Bill 1X and the Emergency Proclamation of the Governor of the State of California dated January 17, 2001 (the "Project"). The Department intends to finance the Project or portions thereof with proceeds of the sale of obligations (the "Obligations"). The Obligations are expected to be issued by the Department. The Department expects to use legally available moneys in order to finance the Project. Prior to the issuance of the Obligations the Department desires to incur certain expenditures (the "Expenditures") with respect to the Project from its own available moneys. The Department has determined that those moneys to be advanced no earlier than 60 days prior to the date of this Declaration to pay the Expenditures are available only for a temporary period and it is necessary to reimburse the Department for the Expenditures from the proceeds of the Obligations if, and when, issued;

2. The reasonably expected maximum principal amount of the Obligations is $6,000,000,000. The Department finds, determines and represents that all the recitals in this Declaration are true and correct.

3. The Department has incurred and will incur costs with respect to the Project prior to the issuance of the Obligations. The Department hereby states its intention and reasonably expects to reimburse such costs with proceeds of the Obligations. The Department may be reimbursed with proceeds of the Obligations for the Expenditures that are paid no earlier than 60 days prior to the date of this Declaration.

4. The Department will make a reimbursement allocation, which is a written allocation that evidences the Department's use of proceeds of the Obligations to reimburse an Expenditure, no later than 18 months after the later of the date on which the Expenditure is paid or the Project is placed in service or abandoned, but in no event more than three years after the date on which the Expenditure is paid. The Department recognizes that exceptions are available for certain "preliminary expenditures," costs of issuance, and certain *de minimis* amounts.

5. Each Expenditure will be either (a) of a type properly chargeable to a capital account under general federal income tax principles (determined in each case as of the date of the Expenditure), (b) a cost of issuance with respect to the Obligations, (c) a nonrecurring item that is not customarily payable from current revenues, or (d) a grant to a party that is not related to or an agent of the Department so long as such grant does not impose any obligation or condition (directly or indirectly) to repay any amount to or for the benefit of the Department.

6. This Declaration is consistent with the budgetary and financial circumstances of the Department, as of the date hereof. To the best of our knowledge, this Department is not aware

of the previous declaration of official intents by the Department that have been made as a matter of course for the purpose of reimbursing expenditures and for which tax-exempt obligations have not been issued.

7. This Declaration is official action of the Department in order to comply with Treasury Regulation §1.150-2 and any other regulations of the Internal Revenue Service relating to the qualification for reimbursement of Department expenditures incurred prior to the date of issue of the Obligations.

Dated: March 9, 2001

Thomas Hannigan
Director, Department of Water Resources
of the State of California

EXHIBIT D

REBATE MEMORANDUM

This Rebate Memorandum addresses matters relating to compliance by the California Department of Water Resources (the "Department") with Section 148(f) of the Internal Revenue Code of 1986, as amended (the "Code"), including regulations issued by the United States Department of the Treasury thereunder. Capitalized terms used herein which are not otherwise defined herein shall have the respective meanings set forth in the Tax Certificate to which this Rebate Memorandum is attached.

1. General. The Department covenants that it will determine precisely what is required with respect to Section 148(f) of the Code and will comply with any requirements applicable to the Tax-Exempt Obligations. The Department acknowledges that, to the extent that an exception to the rebate requirements of Section 148(f) of the Code is not available with respect to the Tax-Exempt Obligations, under Section 148(f) of the Code, the federal government must be paid the sum of (i) the excess of the amount earned on all "nonpurpose investments" with respect to the Tax-Exempt Obligations over the amount that would have been earned had such investments been invested at a rate equal to the yield with respect to the Tax-Exempt Obligations, plus (ii) any income attributable to the excess described in clause (i) (the "Rebate Requirement").

The Department acknowledges that currently, unless an exception to the Rebate Requirement is available, compliance with Section 148(f) of the Code generally involves a multi-step process: (1) ascertaining the funds (the "Gross Proceeds") and investments (the "Nonpurpose Investments") subject to the Rebate Requirement of Section 148(f) of the Code after applying, if applicable, a universal cap with respect to the Tax-Exempt Obligations (the "Universal Cap"), (2) creating an investment history cash flow report with respect to the investment of Gross Proceeds of the Tax-Exempt Obligations, (3) determining the yield with respect to the Tax-Exempt Obligations (the "Yield"), (4) future valuing receipts and payments in the cash flow report (including certain deemed receipts and payments) using the Yield as the discount factor, and (5) determining the amount of rebatable arbitrage with respect to the Tax-Exempt Obligations and paying the appropriate amount to the United States Treasury. See Treas. Reg. Sections 1.148-0 through 1.148-11, 1.149(d)-1, and 1.150-1 for rules with respect to rebate compliance methodology. See Section 2.1 hereof for a description of Nonpurpose Investments with respect to the Tax-Exempt Obligations, Section 2.2 hereof for a description of Gross Proceeds of the Tax-Exempt Obligations, Section 2.3 hereof for the description of a Universal Cap with respect to the Tax-Exempt Obligations, Section 2.4 hereof for a description of Yield with respect to the Tax-Exempt Obligations for purposes of compliance with Section 148(f) of the Code, and Sections 4 and 5 hereof with respect to allocating Gross Proceeds, recordkeeping, and permitted investment of Gross Proceeds.

The Department also acknowledges that additional or different requirements may be applicable to the Tax-Exempt Obligations if certain exceptions are satisfied. See Section 3 herein.

2. Operative Terms.

2.1 Nonpurpose Investments. Subject to the limitation in Section 2.3 hereof, Nonpurpose Investments are generally securities, obligations, annuity contracts or any other investment-type property that are not acquired to carry out the governmental purpose of the Tax-Exempt Obligations that are allocated to Gross Proceeds. However, Nonpurpose Investments do not include:

2.1.1 United States Treasury - State and Local Government Series, Demand Deposit Securities; or

2.1.2 Tax-Exempt Investments. The term "tax-exempt investments" for the purposes of this Tax Certificate includes only obligations the interest on which is excludable from gross income for federal income tax purposes that do not constitute "specified private activity bonds" for purposes of Section 57(a)(5)(C) of the Code. The term "tax-exempt investments" does, however, include stock in a "qualified regulated investment company," which is a corporation that (A) is a regulated investment company within the meaning of Section 851(a) of the Code and meets the requirements of Section 852(a) of the Code for the taxable year; (B) has only one class of stock authorized and outstanding; (C) invests all of its assets in tax-exempt investments (as defined above) to the extent practicable; and (D) has at least 98% of its gross income derived from interest on, or gain from the sale or other disposition of, tax-exempt obligations or at least 98% of the weighted average value of its assets is represented by investments in tax-exempt investments.

2.2 Gross Proceeds. Subject to the limitation in Section 2.3 hereof, "Gross Proceeds" with respect to the Tax-Exempt Obligations means:

2.2.1 amounts actually or constructively received from the sale (or other disposition) of the Tax-Exempt Obligations;

2.2.2 amounts actually or constructively received from investing amounts described in Section 2.2.1 hereof;

2.2.3 amounts (other than proceeds derived from the sale of the Tax-Exempt Obligations) that are reasonably expected to be or are in fact used to pay debt service with respect to the Tax-Exempt Obligations;

2.2.4 amounts pledged as security for the payment of debt service with respect to the Tax-Exempt Obligations or otherwise serving as a reserve fund with respect to the Tax-Exempt Obligations;

2.2.5 "transferred proceeds" of the Tax-Exempt Obligations; and

2.2.6 any other amounts which are replacement proceeds of the Tax-Exempt Obligations within the meaning of Treasury Regulation Section 1.148-1(c).

2.3 Universal Cap. Except as provided below, in no event shall the value of Nonpurpose Investments allocated to Gross Proceeds of the Tax-Exempt Obligations exceed the Universal Cap of the Tax-Exempt Obligations computed in accordance with Section 1.148-6 of the Treasury Regulations. The Universal Cap of the Tax-Exempt Obligations are equal to the value of

the outstanding Tax-Exempt Obligations computed in accordance with Section 1.148-4 of the Treasury Regulations. The value of a Nonpurpose Investment on a date allocated to Gross Proceeds of the Tax-Exempt Obligations for this purpose is equal to the value of such investment in accordance with Section 1.148-5(d) of the Treasury Regulations. The Universal Cap value and the value of Nonpurpose Investments are to be computed as of the first day of each Bond Year that commences after the second anniversary of the issue date and if the applicable obligations, are a refunding issue, as of each date that, without regard to the Universal Cap, proceeds of any refunded issue become "transferred proceeds" of the Tax-Exempt Obligations within the meaning of Section 1.148-9 of the Treasury Regulations (a "Cap Computation Date"). Amounts described in Section 3.1 hereof are not subject to the Universal Cap. Between Cap Computation Dates, Nonpurpose Investments cease to be allocated to the Tax-Exempt Obligations to the extent they are expended or otherwise cease to be allocated to the Tax-Exempt Obligations under Section 1.148-6 of the Treasury Regulations. To the extent Nonpurpose Investments cease to be allocated to the Tax-Exempt Obligations, other investments become so allocated up to the amount of the unused Universal Cap, computed in accordance with Section 1.148-6 of the Treasury Regulations. If on a Cap Computation Date Nonpurpose Investments have a value in excess of the Universal Cap, an amount of such investments necessary to eliminate that excess ceases to be allocated to the Tax-Exempt Obligations. Nonpurpose Investments cease to be allocated to the Tax-Exempt Obligations in the following order, within the meaning of Section 1.148-6 of the Treasury Regulations:

•first, amounts held in a sinking fund, pledged fund, or reserve or replacement fund for the Tax-Exempt Obligations (other than proceeds derived from the sale of the Tax-Exempt Obligations),

•second, "transferred proceeds", and

•third, proceeds derived from the sale of the Tax-Exempt Obligations and earnings thereon, all within the meaning of Section 1.148-6 of the Treasury Regulations.

A failure to do a Universal Cap calculation on a Cap Computation Date will not result in noncompliance with Section 148(f) of the Code if, in the absence of that failure, the Tax-Exempt Obligations would have satisfied the Rebate Requirement.

3. Rebate Exceptions.

3.1 Debt Service Fund. As the Tax-Exempt Obligations do not have an average maturity of greater than 5 years, amounts earned on moneys in the Bona Fide Debt Service Funds (other than pre-issuance accrued interest, if any) shall not be taken into account for a Bond Year for purposes of complying with the Rebate Requirement to the extent that the aggregate amount of earnings on such amounts in such funds is less than $100,000 for such Bond Year. All earnings on amounts in the Bona Fide Debt Service Funds shall be taken into account for purposes of calculating the Rebate Requirement to the extent that earnings exceed $100,000 in such Bond Year.

3.2 Expenditure Exceptions. There are two expenditure exceptions from the Rebate Requirement - the "Six-Month Exception" and the "Eighteen-Month Exception." The Department will be relieved of the obligation to pay the Rebate Requirement with respect to that portion of the proceeds of the Tax-Exempt Obligations described in each applicable Subsection.

3.2.1 Six-Month Exception. The Department will be relieved of the obligation to pay the Rebate Requirement with respect to the portion of the proceeds of the Tax-Exempt Obligations described in Section 3.2.2.1 below if the requirements described in Section 3.2.2.2 are satisfied.

3.2.2.1 Applicability. All Gross Proceeds of the Tax-Exempt Obligations (other than "transferred proceeds" of the Tax-Exempt Obligations, amounts held in a reasonably required reserve fund, if any, and amounts described in Section 3.1 of this Tax Certificate), are described in this Section.

3.2.2.2 Qualification. This exception will be treated as having been satisfied if all Gross Proceeds of the Tax-Exempt Obligations subject to this exception are expended for the governmental purposes of the Tax-Exempt Obligations no later than the day that is six months after the date of issue of the Tax-Exempt Obligations.

3.2.3 Eighteen-Month Exception. The Department will be relieved of the obligation to pay the Rebate Requirement with respect to the portion of the proceeds of the Tax-Exempt Obligations described in Section 3.2.3.1 below if the requirements described in Section 3.2.3.2 are satisfied.

3.2.3.1 Applicability. All Gross Proceeds of the Tax-Exempt Obligations allocable to new money purposes that may be invested at an unrestricted yield, including reasonably expected investment earnings as of the date hereof (other than amounts described in Section 3.1 of this Tax Certificate, and amounts held in a reasonably required reserve fund, if any), are described in this Section. See, Treas. Reg. Sections 1.148-7(c)(3) and (d)(3).

3.2.3.2 Qualification. This exception will be treated as being satisfied if at least 15% of such moneys are expended for the governmental purposes of the Tax-Exempt Obligations within the six-month period beginning on the date of issue of the Tax-Exempt Obligations, at least 60% of such moneys are expended for the governmental purposes of the Tax-Exempt Obligations within the one-year period beginning on the date of issue of the Tax-Exempt Obligations, and 100% of such moneys are expended for the governmental purpose of the Tax-Exempt Obligations within the 18-month period beginning on the date of issue of the Tax-Exempt Obligations. The requirement that 100% of the Gross Proceeds be expended within 18 months may be reduced to not below five percent (5%) of the proceeds derived from the sale of the Tax-Exempt Obligations subject to this exception that is retained for reasonable business purposes relating to the property financed with the Tax-Exempt Obligations provided such moneys are expended within 30 months of the issue date of the Tax-Exempt Obligations. Additionally, the requirement that 100% of the Gross Proceeds be expended within 18 months may be reduced by an amount equal to the lesser of 3% of the issue price of the Tax-Exempt Obligations or $250,000.00 if the Department exercised due diligence to complete the Project.

4. Recordkeeping and Allocation of Gross Proceeds. The Department shall maintain or cause to be maintained detailed records with respect to each security, obligation, annuity contract, or any other investment-type property allocated to Gross Proceeds, including: (i) purchase date, (ii) purchase price, (iii) information establishing fair market value on the date such investment is allocated to Gross Proceeds, (iv) any accrued interest paid, (v) face amount, (vi) coupon rate, (vii) periodicity of interest payments, (viii) disposition price, (ix) any accrued interest received, and

(x) disposition date. Such detailed recordkeeping is required to facilitate the calculation of the Rebate Requirement. The Department shall establish separate sub-accounts or take other accounting measures in order to account fully for all Gross Proceeds.

The Department may use any reasonable, consistently applied accounting method to account for Gross Proceeds in accordance with Treasury Regulation Section 1.148-6. An accounting method is consistently applied if such method accounts uniformly for (i) Gross Proceeds commingled with other moneys in excess of $25,000.00 and such other commingled moneys and (ii) Gross Proceeds for each fiscal year or interim fiscal period therein during which the issue is outstanding. Another accounting method may, however, be utilized for moneys if it is for a bona fide purpose unrelated to federal income tax restrictions. For purposes of allocating Gross Proceeds to capital expenditures intended to be financed pursuant to this Tax Certificate after the date of issue of the applicable tax-exempt obligation, and paid to unrelated third parties ("Qualified Capital Expenditures"), the Department may use the following accounting methods: "specific tracing," "gross-proceeds-spent-first," "first-in, first-out," or a ratable allocation method. The Department covenants to consult with nationally-recognized bond counsel with respect to the applicable method of allocation of Gross Proceeds to expenditures that are not Qualified Capital Expenditures.

If Gross Proceeds are commingled with other moneys (other than in an open-end regulated investment company) in an amount in excess of $25,000.00 (a "Commingled Fund"), the following additional requirements must be satisfied. First, all payments and receipts with respect to investments in the Commingled Fund must be allocated among the different moneys ratably based upon either (i) average daily balances during a "Computation Period" (as defined below) or (ii) the average of the beginning and ending balances of the amounts in the Commingled Fund for a Computation Period that does not exceed one month. A Commingled Fund may use as its Computation Period any consistent time period within its fiscal year that does not exceed three months. Not less frequently than at the end of each Computation Period, the Commingled Fund must compute and allocate to different types of moneys all payments, receipts, income, gain or losses realized, and expenditures. Second, except as provided below, the Commingled Fund must treat all of its investments as if sold at fair market value on the last day of the fiscal year or as of the last day of each Computation Period, and so allocate net gains or losses from such deemed sales (the "Mark-to-Market Requirement"). A Commingled Fund need not satisfy the Mark-to-Market Requirement if (i) the remaining weighted average maturity of all investments held by the Commingled Fund during a fiscal year does not exceed eighteen months and such investments consist exclusively of debt obligations, (ii) the Commingled Fund serves as a common reserve fund or sinking fund for two or more issues of the same issuer, or (iii) the Department (and any related party) do not own more than twenty-five percent of beneficial interests in the Commingled Fund. Common reserve funds or sinking funds for two or more issues must be ratably allocated (not less frequently than once every five years and on each date a new issue is added or retired (if relative original principal amounts are used to so allocate)) in accordance with (i) the value of the bonds under Treasury Regulation Section 1.148-4(e), (ii) the relative amounts of the remaining maximum annual debt service payable on the issues, or (iii) the relative original stated principal amounts of the outstanding issues. Notwithstanding any other provision of this Tax Certificate, the allocation methodology applied must be consistent for all purposes of this Tax Certificate.

The Department must account for the allocation of Gross Proceeds to expenditures not later than eighteen months after the later of the date the expenditure is paid and the date the applicable project is placed in service and in any event, by the date sixty days after the fifth anniversary of the

issue date of the Tax-Exempt Obligations or the date 60 days after the retirement of the Tax-Exempt Obligations, if earlier.

5. Prohibited Investments and Dispositions. The Department acknowledges that compliance with Section 148(f) of the Code may involve taking no action to artificially reduce the Rebate Requirement by the manner of investing Gross Proceeds. The Department covenants that absent an opinion of nationally-recognized bond counsel that the exclusion from gross income of interest with respect to the Tax-Exempt Obligations will not be adversely affected, it will comply with the rules of this Section 5 to assure compliance with Section 148(f) of the Code.

5.1 General Rule. Except to the extent imputed receipts would not arise under Section 1.148-5 of the Treasury Regulations, no Nonpurpose Investment may be acquired with Gross Proceeds for an amount (including transaction costs, except as otherwise provided in Section 1.148-5(e) of the Treasury Regulations) in excess of the fair market value of such Nonpurpose Investment. No Nonpurpose Investment may be sold or otherwise disposed of for an amount (including transaction costs, except as otherwise provided in Section 1.148-5(e) of the Treasury Regulations) less than the fair market value of the Nonpurpose Investment.

5.2 Fair Market Value. In general, the fair market value of any Nonpurpose Investment is the price which a willing buyer would pay to a willing seller to acquire the Nonpurpose Investment, with no amounts to artificially reduce or increase the yield on the Nonpurpose Investment. The following provisions provide guidelines as to when the Nonpurpose Investment will be deemed to be acquired for its fair market value. Other methods may be used, however, to establish fair market value, so long as those methods comply with the requirements of Section 1.148-5(d)(6) of the Treasury Regulations.

5.3 Investment Contracts. Nonpurpose Investments that are investment contracts (within the meaning of Section 1.148-5(d)(6)(iii) of the Treasury Regulations) will be considered acquired and disposed of for an amount equal to the fair market value of such obligations if the following Sections are satisfied:

5.3.1 a bona fide solicitation is made for the Nonpurpose Investment with specified material terms and at least three bids on the Nonpurpose Investment are received from different reasonably competitive providers of the Nonpurpose Investment other than those with a material financial interest in the Tax-Exempt Obligations (*e.g.*, the purchaser or underwriter);

5.3.2 the yield (determined net of broker's fees) on the Nonpurpose Investment is at least equal to the yield offered under the highest bid received from a noninterested party (or the Department has significant bona fide non-tax reasons, such as creditworthiness of the bidder, for failure to purchase the highest yielding investment);

5.3.3 the yield on the Nonpurpose Investment (determined net of broker's fees) is not less than the yield then currently available from the provider or reasonably comparable investments offered to other persons, if any, from a source of funds other than Gross Proceeds of tax-exempt obligations;

5.3.4 the price of the Nonpurpose Investment takes into account as a significant factor the Department's reasonably expected draw-down schedule, exclusive of float funds and reasonably required reserve funds;

5.3.5 the terms of the Nonpurpose Investment, including the collateral security requirements for the Nonpurpose Investment, are reasonable; and

5.3.6 the obligor of the Nonpurpose Investment certifies the administrative costs that are reasonably expected to be paid to third parties in connection with the Nonpurpose Investment.

5.4 Certificates of Deposit. Nonpurpose Investments that are certificates of deposit with a fixed interest rate, a fixed principal payment schedule, a fixed maturity, and a substantial penalty for early withdrawal, will be considered acquired for their fair market value if the following requirements are satisfied:

5.4.1 the yield on the certificate of deposit is not less than the yield on reasonably comparable direct obligations of the United States; and

5.4.2 the yield on the certificate of deposit is not less than the highest yield that is published or posted by the provider to be currently available from the provider on comparable certificates of deposit offered to the public.

5.5 Arm's Length Purchase and Sale. Except as described above, the fair market value of any Nonpurpose Investment for which there is an established market shall be determined as provided in this Section 5.5. Any market especially established to provide Nonpurpose Investments to an issuer of governmental obligations shall not be treated as an established market.

5.5.1 If a Nonpurpose Investment is acquired pursuant to an arm's length transaction without regard to any amount paid to reduce the yield on the Nonpurpose Investment, the fair market value of the Nonpurpose Investment shall be the amount paid for the Nonpurpose Investment (without an increase for transaction costs except as provided infra).

5.5.2 If a Nonpurpose Investment is sold or otherwise disposed of in an arm's length transaction without regard to any reduction in the disposition price to reduce the amount due under Section 148(f) of the Code, the fair market value of the Nonpurpose Investment shall be the amount realized from the sale or other disposition of the Nonpurpose Investment (without reduction for transaction costs except as provided infra).

5.5.3 If a United States Treasury obligation is acquired directly from or disposed of directly to the United States Treasury (as in the case of State and Local Government Series ("SLGs") obligations), such acquisition or disposition shall be treated as establishing a market for the obligation and as establishing the fair market value of the obligation.

5.5.4 Alternatively, the fair market value of any Nonpurpose Investment for which there is an established market may be set at the mean of the bid and offered prices on an established market where such Nonpurpose Investment is traded on the date a binding contract to acquire such Nonpurpose Investment is entered into, or, if there are no bid and offered prices on such

date, on the first day preceding such date for which there are bid and offered prices. Such mean price may be determined by reference to any appropriate publication, such as, for example, "Composite Closing Quotations for United States Government Securities" published by the Federal Reserve Bank of New York. Where the price of any Nonpurpose Investment is quoted on an established market in terms of yield, the fair market value shall be the amount necessary to produce such yield.

5.5.5 The fair market value of Nonpurpose Investments may also be established by the borrowing practices of the issuer of such Nonpurpose Investments, as, for example, by determining the fair market value based on the interest ordinarily paid by such issuer to persons other than governmental units with respect to Nonpurpose Investments of comparable maturities.

5.6 Non-Arm's Length Transactions. Except to the extent the requirements of Section 3 hereof are met, any Nonpurpose Investment for which there is no established market shall be rebuttably presumed to be for an amount in excess of the fair market value of the Nonpurpose Investment.

5.7 Administrative Costs. The purchase or sales price of a Nonpurpose Investment is not adjusted (except as provided below) to take into account any administrative costs of the Nonpurpose Investment. Certain administrative costs, including reasonable direct administrative costs, other than carrying costs, such as brokerage commissions or selling commissions, but not legal and accounting fees, recordkeeping, custody and similar costs, may be taken into account in computing the Rebate Requirement with respect to investments. See Treas. Reg. Section 1.148-5(e). General overhead costs and similar indirect costs of the Department such as employee salaries and office expenses and costs of computing rebatable arbitrage may not be taken into account.

5.8 Brokerage Commissions. Compensation received by a broker in connection with the acquisition of any Nonpurpose Investment shall be treated as set forth in Section 1.148-5(e) of the Treasury Regulations. A brokerage commission for an investment contract is included as a receipt with respect to the investment contract (*i.e.*, additional earnings to the Department) to the extent the commission exceeds 0.05 percent of the weighted average amount reasonably expected to be invested each year of the term of the contract.

6. Bond Year. The Department may select any date that is within one year of the date hereof as the day on which each Bond Year ends. If the Department does not select such a date before the earlier of (i) the final maturity date of the Tax-Exempt Obligations, or (ii) June 26, 2006, then for purposes of this Tax Certificate the term "Bond Year" shall mean each one-year (or shorter) period ending on each June 26 until there is no outstanding Tax-Exempt Obligations.

CERTIFICATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES
PURSUANT TO CREDIT AND SECURITY AGREEMENT
SECTION 4.1(j)

The California Department of Water Resources (the "Department") hereby certifies as follows:

1. This Certificate is issued pursuant to Section 4.1(j) of the Credit and Security Agreement, dated as of June 26, 2001, among the State acting through the Department of Water Resources, various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). Terms used but not defined herein shall have the respective meanings ascribed thereto in the Agreement.

2. Other than events that have been disclosed in writing to the Lenders by or on behalf of the Department, no material adverse condition or material adverse change (including change in law, rule or regulation or lawsuit) has occurred or become known to the Department since April 3, 2001 that could, in the opinion of the Department, reasonably be expected to adversely affect the Department's ability to timely perform its obligations under the Transaction Documents.

Dated: June 26, 2001.

CALIFORNIA DEPARTMENT OF
WATER RESOURCES

By _____
Thomas M. Hannigan
Director

This SYNDICATION AGREEMENT (this "Agreement"), dated as of June 26, 2001, is entered by and among J.P. MORGAN SECURITIES INC., as lead arranger and book manager of the Credit Agreement (as defined below) (in such capacity, together with any successor appointed thereunder, or successor by means of merger, the "Arranger"), the financial institutions from time to time party to this Agreement (each a "Syndicating Lender" and collectively, the "Syndicating Lenders"), and MORGAN GUARANTY TRUST COMPANY OF NEW YORK, in its capacity as agent under the Credit Agreement described below (in such capacity, together with any successor appointed thereunder, or successor by means of merger, the "Agent").

W I T N E S S E T H:

WHEREAS, pursuant to the Credit and Security Agreement dated as of the date hereof (as amended, supplemented, restated or otherwise modified from time to time, the "Credit Agreement"), among the State of California acting through its Department of Water Resources (the "Department"), the financial institutions from time to time party thereto and the Agent, the Syndicating Lenders have agreed to make available to the Department a loan or loans in the amount of their respective Commitment (as defined in the Credit Agreement) (each, a "Loan", and, collectively, the "Loans"); and

WHEREAS, in order to assure an orderly, coordinated and equitable syndication of the Loans and the rights and obligations of the Syndicating Lenders under the Credit Agreement, the Arranger, the Syndicating Lenders and the Agent desire to set forth the procedures to be adhered to by all the Syndicating Lenders, the Arranger and the Agent during the Syndication Period (as defined below).

NOW, THEREFORE, IT IS AGREED:

SECTION 1. DEFINITIONS AND PRINCIPLES OF CONSTRUCTION

1.1 Definitions. Unless otherwise defined herein, capitalized terms used herein shall have the meanings given thereto in the Credit Agreement. 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):

"Assigned Share" shall mean (a) with respect to an Assignee, that percentage interest of the Loans assumed by such Assignee and (b) with respect to a Syndicating Lender, that percentage interest of the Loans assigned by such Syndicating Lender, in each case, pursuant to the terms of the Assignment and Acceptance Agreement.

"Assignee" and "Assignees" shall have the meanings provided in Section 3.2.

"Assignment and Acceptance Agreement" shall have the meaning provided in Section 4.5.

"Assignment Notice" shall have the meaning provided in Section 4.1.

"Assignment Pool A" shall have the meaning provided in Section 2.1(a).

"Assignment Pool B" shall have the meaning provided in Section 2.1(b).

"Contribution" shall mean for each Syndicating Lender, at any time and as the context requires, its Taxable Loan Contribution, Tax-Exempt Loan Contribution or all such contributions.

"Insured Loans" shall mean, for each Syndicating Lender, the Loans with respect to which such Syndicating Lender, as of the Term Out Period Commencement Date and for the full Term Out Final Period, has obtained credit enhancement.

"Lender Affiliate" shall have the meaning provided in the Credit Agreement.

"Loan Assignment Amount" shall mean the sum of the Assigned Shares of Loans of each of the Assignees.

"Loan Payment" shall have the meaning provided in Section 5.

"Person" shall mean any individual, partnership, limited liability company, joint venture, firm, corporation, association, trust or other enterprise or any government or political subdivision or any agency, department or instrumentality thereof.

"Pre-sold Loans" shall mean, for a Syndicating Lender on any date of determination, the sum of (a) the aggregate principal amount of the Loans of such Syndicating Lender sold and assigned by such Syndicating Lenders to Persons other than Lender Affiliates of such Syndicating Lender through such date, and (b) the aggregate principal amount of all participation interests in Loans sold by such Syndicating Lenders to Persons other than Lender Affiliates of such Syndicating Lender through such date.

"Syndication Period" shall mean the period commencing on the Term Out Period Commencement Date and ending at 4:00 p.m., New York City time, on the ninetieth day after the Term Out Period Commencement Date.

"Target Hold Level" shall mean, for each Syndicating Lender, the amount, if any, agreed to between the Syndicating Lender and the Department, which amount is set forth opposite the name of such Syndicating Lender on Schedule 1 hereto.

"Taxable Assignment Amount" means the sum of the commitments of each of the Assignees to assume Taxable Loans.

"Taxable Loan Contribution" shall mean for each Syndicating Lender, at any time, the amount set forth opposite such Syndicating Lender's name in Schedule 1 under the heading "Taxable Loan Contribution" as such amount may from time to time be reduced pursuant to Section 2.

"Tax-Exempt Assignment Amount" means the sum of the commitments of each of the Assignees to assume Tax-Exempt Loans.

"Tax-Exempt Loan Contribution" shall mean for each Syndicating Lender, at any time, the amount set forth opposite such Syndicating Lender's name in Schedule 1 under the heading "Tax-Exempt Loan Contribution" as such amount may from time to time be reduced pursuant to Section 2.

1.2 Principles of Construction

(a) The principles of construction set forth in subparagraphs (a) through (j) and subparagraph (l) of Section 1.2 of the Credit Agreement are, by this reference, incorporated herein as if set forth in their entirety, provided that references to the "Transaction Documents" shall mean this Agreement.

(b) This Agreement is the result of negotiations among and has been reviewed by counsel to the Arranger, the Agent, and the Syndicating Lenders, and is the product of all parties. Accordingly, this Agreement shall not be construed against a party merely because of that party's involvement in its preparation.

SECTION 2. CREATION OF ASSIGNMENT POOL

2.1 Initial Contributions

(a) Subject to, and upon, the terms and conditions set forth herein, each Syndicating Lender severally agrees, during the Syndication Period, to assign its Taxable Loans in an amount not to exceed its Taxable Loan Contribution. The Arranger will aggregate the Taxable Loan Contributions of the Syndicating Lenders in an assignment pool, which shall be referred to herein as "Assignment Pool A" and as may be modified from time to time pursuant to this Agreement.

(b) Subject to, and upon, the terms and conditions set forth herein, each Syndicating Lender severally agrees, during the Syndication Period, to assign its Tax-Exempt Loans in an amount not to exceed its Tax-Exempt Loan Contribution. The Arranger will aggregate the Tax-Exempt Loan Contributions of the Syndicating Lenders in an assignment pool, which shall be referred to herein as "Assignment Pool B" and as may be modified from time to time pursuant to this Agreement.

(c) If, after the date of this Agreement and prior to commencement of the Syndication Period, an Additional Lender becomes a Lender under the Credit Agreement, such Additional Lender may become a Syndicating Lender under this Agreement by executing and delivering to the Agent a Joinder to this Agreement in accordance with Section 6.9. Subject to the first sentence of Section 2.2(c) and promptly following its receipt of an executed Joinder to this Agreement, the Agent shall include such Syndicating Lender's Contribution in Assignment Pool A and/or Assignment Pool B, as the case may be, and shall prepare and deliver to each Syndicating Lender a revised Schedule 1, reflecting the new Contributions of the Syndicating Lenders.

2.2 Adjustments to Contributions

(a) Subject to Section 2.2(c) and upon at least one Business Day's prior written notice to the Agent, each Syndicating Lender shall have the right to reduce or modify its Contribution in whole or in part, in integral multiples of $10,000,000.

(b) Subject to Section 2.2(c), in the event that the Loans of any Syndicating Lender are prepaid in part pursuant to the Credit Agreement, the Agent shall proportionately adjust the Contribution of such Syndicating Lender to reflect such prepayment.

(c) Unless otherwise approved by the Arranger, no Contribution of any Syndicating Lender shall at any time exceed (i) the aggregate unpaid principal amount of the Loans of such Syndicating Lender less (ii) the Target Hold Level of such Syndicating Lender less (iii) the aggregate unpaid principal amount of the Insured Loans and Pre-sold Loans of such Syndicating Lender. Upon making any adjustment to the Contribution of any Syndicating Lender under Section 2.2(a), (b) or (c), the Agent shall promptly adjust Assignment Pool A and/or Assignment Pool B, as the case may be, and prepare and deliver to each Syndicating Lender a revised Schedule 1, reflecting the adjusted Contributions of the Syndicating Lenders.

SECTION 3. ROLE OF THE ARRANGER; CLEAR MARKET

3.1 The Arranger shall manage all aspects of the syndication of the Loans and the syndication of the rights and obligations of the Syndicating Lenders under the Credit Documents.

3.2 The Arranger, with such assistance from other Syndicating Lenders as may be offered and requested, will solicit indications of interest in purchasing portions of Assignment Pool A and Assignment Pool B from other commercial lenders, financial institutions and accredited investors (each an "Assignee" and collectively, the "Assignees").

3.3 During the Syndication Period, except for (a) assignments made pursuant to this Agreement or (b) sales of participation interests made with the prior approval of the Arranger, each Syndicating Lender agrees not to sell, assign, transfer, convey or grant any interest in (including by way of participation) its Loans or rights and obligations under Credit Agreement. Prior to the termination of the Syndication Period, each Syndicating Lender agrees to notify the Arranger of the dollar amount of all sales or assignments of Loans made by such Syndicating Lender to Persons other than Lender Affiliates of such Syndicating Lender and the dollar amount of all sales of participation interests in Loans made by such Syndicating Lender to Persons other than Lender Affiliates of such Syndicating Lender.

SECTION 4. ASSIGNMENT PROCESS

4.1 Upon an Assignee's agreeing to purchase all or a portion of Assignment Pool A and/or Assignment Pool B, the Arranger will arrange for such Assignee to execute and deliver to the Agent, with a copy to the Department, a written notice in the form of Exhibit A to this Agreement (an "Assignment Notice").

4.2 From time to time during the Syndication Period and at the close of the Syndication Period, the Arranger will, in its sole discretion, allocate the Assigned Share of Loans of the Assignees among the Taxable Loan Contribution and Tax-Exempt Contribution of the Syndicating Lenders and will notify the Syndicating Lenders and the Assignees of any such determination.

4.3 Subject to, and upon, the terms and conditions set forth herein, each Syndicating Lender hereby agrees to assign its Percentage of the Taxable Assignment Amount. For purposes of this Section 4.3 only, "Percentage" shall mean, for each Syndicating Lender, that percentage (expressed as a decimal) obtained by dividing the amount of its Taxable Contribution by Assignment Pool A.

4.4 Subject to, and upon, the terms and conditions set forth herein, each Syndicating Lender hereby agrees to assign its Percentage of the Tax-Exempt Assignment Amount. For purposes of this Section 4.4 only, "Percentage" shall mean, for each Syndicating Lender, that percentage (expressed as a decimal) obtained by dividing the amount of its Tax-Exempt Contribution by Assignment Pool B.

4.5 The Agent will coordinate the execution by the Assignees, Syndicating Lenders, and the Department of an Assignment and Acceptance Agreement (the "Assignment and Acceptance Agreement") in the form of Exhibit B to this Agreement. The Assignment and Acceptance Agreement shall reflect the terms and conditions of each Assignee's Assignment Notice and this Agreement.

SECTION 5. PAYMENTS

Each Syndicating Lender hereby acknowledges that, under Section 3.1 of the Assignment and Acceptance Agreement, that each Assignee will agree to pay to the Agent, on the Effective Date and for the account of the Syndicating Lenders, the principal amount of any Loans which are outstanding on the Effective Date and which are included within such Assignee's Assigned Share of Loans. Each party hereby agrees that, upon the Agent's receipt of any such payment (each a "Loan Payment"), the Agent shall distribute such Loan Payment on the same day to each Syndicating Lender on the basis of such Syndicating Lender's Percentage of the Loan Payment; provided that if a Loan Payment is received by the Agent after 2:00 p.m., New York City time, on a Business Day, the Agent will make such payment available to the Syndicating Lenders by 12:00 noon, New York City time, on the next Business Day. For purposes of this Section 5 only, "Percentage" shall mean, for each Syndicating Lender, that percentage (expressed as a decimal) obtained by dividing the amount of its Assigned Share of Loans by the Loan Assignment Amount.

SECTION 6. MISCELLANEOUS

6.1 Promptly, and in any event within two Business Days after any Syndicating Lender obtains credit enhancement in respect of any Loan made by such Syndicating Lender, such Syndicating Lender shall give notice thereof, including the outstanding principal amount of any such Loan and the type, amount and period of credit enhancement, to the Arranger and the Agent.

6.2 Each party hereby agrees from time to time, upon the request of any other party, to take such additional actions and to execute and deliver such additional documents and instruments as such other party may reasonably request to effect the transactions contemplated by, and to carry out the intent of, this Agreement.

6.3 Neither this Agreement nor any term hereof may be changed, waived, discharged or terminated, except by an instrument in writing signed by the party (including, if applicable, any party required to evidence its consent to or acceptance of this Agreement) against whom enforcement of such change, waiver, discharge or termination is sought.

6.4 Unless otherwise specifically provided herein, any notice or other communication herein required or permitted to be given shall be in writing and may be personally served, telexed or sent by facsimile or United States mail or courier service and shall be deemed to have been given when delivered in person or by courier service, upon receipt of facsimile or telex, or three Business Days after deposit in the United States mail with postage prepaid and properly addressed. For the purposes hereof, the notice address of each Syndicating Lender shall be as set forth on the records of the Agent or, as to any such party, such other address as shall be designated by such party in a written notice delivered to the other parties.

6.5 In case any provision in or obligation under this Agreement shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provision or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

6.6 **THIS AGREEMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF CALIFORNIA.**

6.7 This Agreement shall be binding upon, and shall inure to the benefit of, the parties hereto and their respective successors and assigns.

6.8 This Agreement may be executed in one or more counterparts and by the different parties hereto in separate counterparts, each of which when so executed and delivered shall be deemed an original, but all such counterparts together shall constitute but one and the same instrument; signature pages may be detached from multiple separate counterparts and attached to a single counterpart so that all signature pages are physically attached to the same document.

6.9 This Agreement shall become effective with respect to each Syndicating Lender, and each Lender shall become a Syndicating Lender with all of the rights and obligations attendant thereto, on the date (the "Joinder Date") on which such Lender shall have executed a joinder in the form of Exhibit C hereto and shall have delivered the same to the Agent and the Agent shall have accepted the same. The Agent will give each Syndicating Lender prompt written notice of the occurrence of a Joinder Date with respect to joinder of each Lender.

IN WITNESS WHEREOF, the parties hereto have caused their duly authorized officers to execute and deliver this Agreement as of the date first above written.

J.P. MORGAN SECURITIES INC., as Arranger

By: Sandra Brinkert
Name: Sandra Brinkert
Title: VP

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK, as Agent and a Syndicating
Lender

By: William P. Hansen

Name: WILLIAM P. HANSEN, JR.
Title: VICE PRESIDENT

JPMORGAN CHASE & CO., as a Syndicating Lender

By: _____
Name: James R. Wise
Title: VP

LEHMAN COMMERCIAL PAPER INC., as a Syndicating Lender

By: _____

Name: Stephen Peters

Title: Managing Director

COMMERZBANK
AKTIENGESELLSCHAFT, New York
Branch, as a Syndicating Lender

By: _____
Name: THOMAS J. CARNEY
Title: Senior Vice President

By: _____
Name: Edward C. Neu
Title: Vice President

BAYERISCHE LANDESBANK
GIROZENTRALE, acting through its
New York Branch, as a Syndicating Lender

By: _____
Name: Scott M. Allison
Title: First Vice President

By: _____
Name: John A. Wain
Title: First Vice President

SCHEDULE 1
TO SYNDICATION AGREEMENT

CONTRIBUTIONS

Lender	Taxable Loan Contribution	Tax-Exempt Loan Contribution	Target Hold Level
Morgan Guaranty Trust Company of New York	*	*	$600,000,000*
JPMorgan Chase & Co.	*	*	*
Lehman Commercial Paper Inc.	--	$400,000,000	$400,000,000
Commerzbank AG	$250,000,000	--	$250,000,000
Bayerische Landesbank Girozentrale	$150,000,000	--	$150,000,000
Totals	$400,000,000*	$400,000,000*	$1,400,000,000*

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* The aggregate Target Hold Level for Morgan Guaranty Trust Company of JPMorgan Chase & Co. is $600,000,000. No allocation has yet been made between these entities or among Taxable Loan Contribution or Tax-Exempt Loan Contribution. These allocations will be made prior to the commencement of the Syndication Period.

EXHIBIT A
TO SYNDICATION AGREEMENT

NOTICE OF ASSIGNMENT

[Date]

TO: Morgan Guaranty Trust Company of New York
60 Wall Street
New York, New York 10260
Attention: [_____]

FROM: [Name and address of Assignee]

CC: The Honorable Philip Angelides
Treasurer of the State of California
Room 110
915 Capitol Mall
Sacramento, California 95814

Thomas M. Hannigan
Director of Water Resources
State of California Department of Water Resources
1416 9th Street, 11th Floor
Sacramento, California 95814

RE: Credit and Security Agreement with the State of California acting through its Department of Water Resources

Ladies and Gentlemen:

Reference is made to Credit and Security Agreement dated as of June 26, 2001 (as amended, supplemented, restated or otherwise modified from time to time, the "Credit Agreement"), among the State of California acting through its Department of Water Resources (the "Department"), the financial institutions from time to time party thereto, and Morgan Guaranty Trust Company of New York (the "Agent"). All capitalized terms used herein and not otherwise defined herein shall have the meaning ascribed thereto in the Credit Agreement.

[Assignee's name] (the "Assignee") is pleased to advise you of its commitment to (a) become party to, and be bound by each of the provisions of the Credit Agreement as a "Lender," and (b) purchase up to $[_____] of Loans from Syndicating Lenders (as such term is defined in Syndication Agreement). The Assignee hereby covenants to execute and deliver to you an Assignment and Acceptance Agreement in the form of Exhibit C to the Syndication Agreement.

So long as no Event of Default or Event of Noncompliance has occurred and is continuing, the Assignee's commitment hereunder is subject to the consent of the Department, such consent not to be unreasonably withheld. The Assignee's commitment hereunder is subject to the consent of the Agent, such consent not to be unreasonably withheld.

This Notice of Assignment is not assignable, is intended to be solely for the benefit of the Syndicating Lenders, the Arranger, the Agent and the Department, and is not intended to confer any benefits upon, or create any rights in favor of, any person other than the Syndicating Lenders, the Arranger, the Agent and the Department. This Notice of Assignment may not be amended or modified except by an instrument in writing signed by the Assignee. This Notice of Assignment may be executed in any number of counterparts, each of which shall be an original, and all of which, when taken together, shall constitute one agreement. Delivery of an executed signature page of this Notice of Assignment by facsimile transmission shall be effective as delivery of manually executed counterpart hereof. This Notice of Assignment is the only agreement that has been entered into among us with respect to the Credit Agreement and sets forth the entire understanding of the Assignee, the Arranger, the Agent and the Department with respect thereto. This Notice of Assignment shall be governed by, and construed in accordance with, the laws of the State of New York, without regard to conflicts of law.

If the foregoing correctly sets forth our agreement, please indicate your acceptance of the terms hereof by returning to us executed counterparts hereof not later than 5:00 p.m., New York City time, on [_____], 2001. The Assignee's commitment herein will expire at such time in the event the Assignee has not received such executed counterparts in accordance with the immediately preceding sentence. In the event you timely accept the commitment set forth in this Notice of Assignment, the commitment hereunder shall automatically terminate at 4:00 p.m., New York City time, on the last day of the Syndication Period, unless the assignment has been effected prior to that time.

Very truly yours,

[Name of Assignee]

By:_____
Name: _____
Title: _____

Accepted and agreed to as of
the date first written above by:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK, as Agent

By:_____
Name: _____
Title: _____

[STATE OF CALIFORNIA,
Acting through its
DEPARTMENT OF WATER RESOURCES

By:_____
Name: _____
Title: _____]

EXHIBIT B
TO SYNDICATION AGREEMENT

ASSIGNMENT AND ACCEPTANCE AGREEMENT

Reference is made to the Credit and Security Agreement dated as of June 26, 2001 (as amended, supplemented, restated or otherwise modified from time to time, the "Credit Agreement"), among the STATE OF CALIFORNIA acting through its DEPARTMENT OF WATER RESOURCES (the "Department"), the financial institutions from time to time party thereto (the "Lenders"), and MORGAN GUARANTY TRUST COMPANY OF NEW YORK, acting in the manner and to the extent described in Section 8 of the Credit Agreement (the "Agent"). Unless otherwise defined herein, capitalized terms used herein shall have the meanings given thereto in the Credit Agreement.

The Agent, each party designated as an Assignor (each an "Assignor" and collectively, the "Assignors") above the signature of such party on the Schedule of Terms attached hereto and hereby made an integral part hereof (the "Schedule of Terms"), and each party designated as an Assignee (each an "Assignee" and collectively, the "Assignees") above the signature of such party on the Schedule of Terms hereby make and enter into this assignment and acceptance agreement (the "Assignment Agreement") as of [_____], 200[_].[1]

IN CONSIDERATION of the agreements, provisions and covenants herein contained, the parties hereto hereby agree as follows:

SECTION 1. ASSIGNMENT AND ASSUMPTION

1.1 Each Assignor hereby sells and assigns to the Assignees without recourse and without representation or warranty (except as expressly set forth herein) that interest in and to all of its rights and obligations under the Credit Documents which represents the percentage interest specified in Item 3 of the Schedule of Terms of the Loans under the Credit Agreement. Each Assignee hereby purchases and assumes from the Assignors that interest in and to all the Assignors' rights and obligations under the Credit Documents which represents the percentage interest specified in Item 4 of the Schedule of Terms of the Loans under the Credit Agreement (each an "Assigned Share" and collectively, the "Assigned Shares").

1.2 Each Assignor and Assignee hereby agrees that, upon the Effective Date (as defined below in Section 3.1), (a) each Assignee shall become a party to the Credit Agreement and shall have all of the rights and obligations of a Lender under the Credit Documents, and shall be deemed to have made all of the covenants and agreements contained in the Credit Documents, arising out of or otherwise related to its Assigned Share, and (b) each Assignor shall be absolutely released as a Lender from any of such obligations, covenants and agreements assumed or made by

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[1] Insert a date, which shall be a Business Day, on or prior to the last day of the Syndication Period.

any Assignee in respect of such Assignee's Assigned Share. Each Assignee hereby acknowledges and agrees that the agreement set forth in this Section 1.2 is expressly made for the benefit of the Department, the Agent, the Assignors and the other Lenders and their respective successors and permitted assigns.

1.3 Each Assignor and each Assignee hereby acknowledges and confirms its understanding and intent that (a) this Assignment and Acceptance Agreement shall effect the assignment by each Assignor and the assumption by each Assignee of the Assignors' rights and obligations with respect to the Assigned Shares, and (b) any other assignments by an Assignor of a portion of its rights and obligations with respect to its Commitment and any Loans shall have no effect on the Loans of any Assignee as set forth in Item 4 of the Schedule of Terms.

SECTION 2. CERTAIN REPRESENTATIONS, WARRANTIES AND AGREEMENTS

2.1 Each party to this Assignment and Acceptance Agreement represents and warrants to the other parties hereto that it has full power and authority to enter into this Assignment and Acceptance Agreement and to perform its obligations hereunder in accordance with the provisions hereof, that this Assignment and Acceptance Agreement has been duly authorized, executed and delivered by such party and that this Assignment and Acceptance Agreement constitutes a legal, valid and binding obligation of such party, enforceable against such party in accordance with its terms, except as enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting creditors' rights generally and by general principles of equity.

2.2 Each Assignor (a) represents and warrants that it is the legal and beneficial owner of the interest being assigned by it hereunder and that such interest is free and clear of any adverse claim; (b) makes no representation or warranty and assumes no responsibility with respect to any statements, warranties or representations made in or in connection with the Credit Documents or the execution, legality, validity, enforceability, genuineness, sufficiency or value of the Credit Documents or any other instrument or document furnished pursuant thereto; and (c) makes no representation or warranty and assumes no responsibility with respect to the financial condition of the Department or the performance or observance by the Department of its obligations under the Credit Documents to which it is a party or any other instrument or document furnished pursuant thereto.

2.3. Each Assignee (a) confirms that it has received a copy of the Credit Agreement, together with copies of the documents and information referred to therein as it has deemed appropriate to make its own credit analysis and decision to enter into this Assignment and Acceptance Agreement; (b) agrees that it will, independently and without reliance upon the Agent, the Assignors or any other Lender and based on such documents and information as it shall deem appropriate at the time, continue to make its own credit decisions in taking or not taking action under the Credit Documents; (c) appoints and authorizes the Agent to take such action as agent on its behalf and to exercise such powers under the Transaction Documents as are delegated to the Agent by the terms thereof, together with such powers as are reasonably incidental thereto; and (d) agrees that it will perform in accordance with their terms all of the obligations which by the terms of the Credit Documents are required to be performed by it as a Lender.

2.4 No Assignor shall be responsible to any Assignee for the execution, effectiveness, genuineness, validity, enforceability, collectibility or sufficiency of any of the Credit Documents or for any representations, warranties, recitals or statements made therein or made in any written or oral statements or in any financial or other statements, instruments, reports or certificates or any other documents furnished or made by it to any Assignee or by or on behalf of the Department to it or any Assignee in connection with the Credit Documents and the transactions contemplated thereby or for the financial condition or business affairs of the Department or any other Person liable for the payment of any Obligations, nor shall any Assignor be required to ascertain or inquire as to the performance or observance of any of the terms, conditions, provisions, covenants or agreements contained in any of the Credit Documents or as to the use of the proceeds of the Loans or as to the existence or possible existence of any Default, Event of Default, Noncompliance or Event of Noncompliance.

SECTION 3. EFFECTIVENESS OF ASSIGNMENT; PAYMENTS

3.1 This Assignment and Acceptance Agreement shall become effective upon the date (the "Effective Date") upon which all of the following conditions are satisfied: (a) the execution of a counterpart hereof by each Assignor and Assignee; (b) the execution of a counterpart hereof by the Agent and, so long as no Event of Default or Event of Noncompliance has occurred and is continuing, the Department as evidence of its acceptance hereof in accordance with Section 9.4 of the Credit Agreement; (c) the receipt by the Agent of originals or facsimiles of the counterparts described above and authorization of delivery thereof, and (d) the receipt by the Agent from each Assignee of a processing fee in the amount of $3,500. The Agent shall notify each Assignee of the Effective Date.

3.2 Each Assignee hereby agrees to pay to the Agent, on the Effective Date and for distribution to the Assignors, the principal amount of any Loans which are outstanding on the Effective Date and which are included within the Assignee's Assigned Share of Loans, in accordance with the applicable payment instructions set forth in Item 6 of the Schedule of Terms. Each Assignee shall be entitled to all interest on its Assigned Share of Loans from the Effective Date at the rates applicable thereto under the Credit Agreement and which accrues on and after the Effective Date, such interest to be paid by the Agent directly to each Assignee. It is further agreed that all payments and prepayments of principal made on an Assigned Share of the Loans which occur on and after the Effective Date will be paid directly by the Agent to the Assignees.

SECTION 4. MISCELLANEOUS

4.1 Each party hereby agrees from time to time, upon the request of any other party, to take such additional actions and to execute and deliver such additional documents and instruments as such other party may reasonably request to effect the transactions contemplated by, and to carry out the intent of, this Assignment and Acceptance Agreement.

4.2 Neither this Assignment and Acceptance Agreement nor any term hereof may be changed, waived, discharged or terminated, except by an instrument in writing signed by the party (including, if applicable, any party required to evidence its consent to or acceptance of this Assignment and Acceptance Agreement) against whom enforcement of such change, waiver, discharge or termination is sought.

4.3 Unless otherwise specifically provided herein, any notice or other communication herein required or permitted to be given shall be in writing and may be personally served, telexed or sent by facsimile or United States mail or courier service and shall be deemed to have been given when delivered in person or by courier service, upon receipt of telefacsimile or telex, or three Business Days after depositing it in the United States mail with postage prepaid and properly addressed. For the purposes hereof, the notice address of each Assignor and each Assignee shall be as set forth on the records of the Agent or, as to any such party, such other address as shall be designated by such party in a written notice delivered to the other parties.

4.4 In case any provision in or obligation under this Assignment and Acceptance Agreement shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provision or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

4.5 **THIS ASSIGNMENT AGREEMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES HEREUNDER SHALL BE GOVERNED BY, AND SHALL BE CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAWS OF THE STATE OF CALIFORNIA.**

4.6 This Assignment and Acceptance Agreement shall be binding upon, and shall inure to the benefit of, the parties hereto and their respective successors and permitted assigns.

4.7 This Assignment and Acceptance Agreement may be executed in one or more counterparts and by different parties hereto in separate counterparts, each of which when so executed and delivered shall be deemed an original, but all such counterparts together shall constitute but one and the same instrument; signature pages may be detached from multiple separate counterparts and attached to a single counterpart so that all signature pages are physically attached to the same document.

IN WITNESS WHEREOF, the parties hereto have caused this Assignment and Acceptance Agreement to be duly executed by their respective officers thereunto duly authorized, as of the date first above written.

SCHEDULE OF TERMS

1. Department: State of California acting through its Department of Water Resources

2. Name and Date of Credit Agreement: Credit and Security Agreement, dated as of June 26, 2001, by and among State of California acting through its Department of Water Resources, the various financial institutions as are or may become parties thereto as Lenders, and Morgan Guaranty Trust Company of New York, as Agent.

[Remainder of page intentionally left blank]

3. **Pre-Settlement**

Lender	Assigned Share of Taxable Loans	Amount of Assigned Share of Taxable Loans	Assigned Share of Tax-Exempt Loans	Amount of Assigned Share of Tax-Exempt Loans
Morgan Guaranty Trust Company of New York	%	$	%	$
JPMorgan Chase & Co.				
Lehman Commercial Paper Inc.	%	$	%	$
Commerzbank AG				
Bayerische Landesbank Girozentrale				
Totals	%	$	%	$

4. **Post-Settlement**

Lender	Assigned Share of Taxable Loans	Amount of Assigned Share of Taxable Loans	Assigned Share of Tax-Exempt Loans	Amount of Assigned Share of Tax-Exempt Loans
[Assignee(s)]	%	$	%	$
	%	$	%	$
	%	$	%	$
Totals	%	$	%	$

[Remainder of page intentionally left blank]

5. Effective Date: [_____], 200[_]

6. Payment Instructions:

On the Effective Date, each Assignee shall wire transfer the sum of the amounts set forth opposite such Assignee's name in Item 4 of this Schedule of Terms under the captions "Amount of Assigned Share of Taxable Loans" and "Amount of Assigned Share of Tax-Exempt Loans" to Morgan Guaranty Trust Company of New York, for distribution to the Assignors, as follows:

Morgan Guaranty Trust Company of New York
c/o Chase Manhattan Bank
ABA No.: 021-000-021
Account No.: 323-2-23788
Account Name: California Department of Water Resources

[Remainder of page intentionally left blank]

7. Signatures:

A. ASSIGNORS:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK, as Lender

By:_____
Name:
Title:

7. Signatures:

A. ASSIGNORS:

JPMORGAN CHASE & CO., as Lender

By:_____
Name:
Title:

7. Signatures:

A. ASSIGNORS:

LEHMAN COMMERCIAL PAPER INC., as
Lender

By:_____
Name:
Title:

7. Signatures:

A. ASSIGNORS:

COMMERZBANK
AKTIENGESELLSCHAFT, New York
Branch, as Lender

By:_____
Name:
Title:

By:_____
Name:
Title:

7. Signatures:

A. ASSIGNORS:

BAYERISCHE LANDESBANK
GIROZENTRALE, acting through its New
York Branch, as Lender

By:_____
Name:
Title:

By:_____
Name:
Title:

7. Signatures:

B. ASSIGNEES:

[insert assignee(s)]

By:_____
Name:
Title:

7. Signatures:

[So long as no Event of Default or Event of Noncompliance has occurred and is continuing:

C. DEPARTMENT:

STATE OF CALIFORNIA
Acting through its
DEPARTMENT OF WATER RESOURCES

By:_____
Name:
Title:]

7. Signatures:

D. AGENT:

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK, as Agent

By:_____
Name:
Title:

EXHIBIT C
TO SYNDICATION AGREEMENT

JOINDER

JOINDER, dated as of the date set forth below, entered into pursuant to the Syndication Agreement, dated as of June 26, 2001(as modified, supplemented, restated, replaced or amended from time to time, the "Syndication Agreement"; capitalized terms used herein but not defined shall have the meanings assigned in the Syndication Agreement), among the Syndicating Lenders listed from time to time on Schedule 1 thereto, Chase Securities Inc., in its capacity as lead arranger and book manager, and Morgan Guaranty Trust Company of New York, in its capacity as agent for the Lenders (the "Agent").

1. Upon acceptance of this Joinder by the Agent, [_____] (the "Additional Lender") (a) shall become a "Syndicating Lender" under the Syndication Agreement, and (b) agrees to be bound by all of the terms and conditions of the Syndication Agreement.

2. **THIS JOINDER SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF CALIFORNIA.**

IN WITNESS WHEREOF, the undersigned has caused this Joinder to be duly executed and delivered by its proper and duly authorized officer(s) as of the date set forth below.

Dated: [_____], 2001

[_____]

By:_____
Name:
Title:

Accepted:

MORGAN GUARANTY TRUST COMPANY OF NEW YORK,
as Agent

By:_____
Title:_____

AGENT RECEIPT OF FEES

Morgan Guaranty Trust Company of New York ("MGT"), as agent for the Lenders under the Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department of Water Resources, various Lenders, and MGT, as Agent (the "Agreement"), hereby acknowledges receipt of all fees due and payable as a condition to closing pursuant to the Agreement.

Dated: June 26, 2001.

MORGAN GUARANTY TRUST
COMPANY OF NEW YORK, as Agent

By William P. Hansen
Name:
Title:

CALIFORNIA DEPARTMENT OF WATER RESOURCES
INCUMBENCY AND SIGNATURE CERTIFICATE

The undersigned, as Director of the California Department of Water Resources (the "Department"), hereby certifies as follows:

1. The persons holding the following positions with the Department are duly appointed and acting as such, and their true and genuine signatures are, as follows:

Name	Position	Signature
Thomas M. Hannigan	Director	
Perla Netto-Brown	Chief, Division of Fiscal Services	
Theresa Lightle	Deputy Comptroller	

2. Each of the persons listed in paragraph 1 is hereby designated an Authorized Representative under the Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department, various Lenders and Morgan Guaranty Trust Company of New York, as Agent, pursuant to Section 1.2(m) thereof.

3. The undersigned has executed each of the following:

A. Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department, various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement").

B. $2,300,000,000 aggregate principal amount of Taxable Bonds (as defined in the Agreement) issued pursuant to the Agreement.

C. $2,000,000,000 aggregate principal amount of Tax-Exempt Bonds (as defined in the Agreement) issued pursuant to the Agreement.

Dated: June 26, 2001.

Thomas M. Hannigan
Director, California Department of Water Resources

The undersigned, as Chief of Fiscal Services of the California Department of Water Resources (the "Department"), hereby certifies as to the matters in paragraph 1 of the above and foregoing Incumbency and Signature Certificate insofar as they relate to the Director of the Department.

Dated: June 26, 2001.

Perla Neto-Bowers
Chief of Fiscal Services, California
Department of Water Resources

CALIFORNIA DEPARTMENT OF WATER RESOURCES AND STATE TREASURER RECEIPT

The California Department of Water Resources (the "Department") hereby acknowledges receipt on the date hereof of the following:

1. $2,300,000,000 proceeds of Taxable Loans made on the date hereof and, without duplication, Taxable Bonds issued on the date hereof, under and pursuant to a Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department, various Lenders, and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"). All terms used and that otherwise defined in this Receipt and Certificate shall have the respective meaning ascribed thereto in the Agreement.

2. $2,000,000,000 proceeds of Tax-Exempt Loans made on the date hereof and, without duplication, Tax-Exempt Bonds issued on the date hereof, under and pursuant to the Agreement.

The Department hereby certifies that the proceeds described above have been deposited as follows:

A. $103,500,000.00 of the amount referred to in paragraph 1 and $90,000,000.00 of the amount referred to in paragraph 2, a total of $193,500,000.00 (the Capitalized Interest and Fees Amount required by the Agreement), has been deposited in the Interest and Fees Account established in the name of Morgan Guaranty Trust Company of New York, as agent for the Lenders, pursuant to Section 2.11(c) of the Agreement.

B. $2,196,500,000.00 of the amount referred to in paragraph 1 and $1,910,000,000.00 of the amount referred to in paragraph 2, a total of $4,106,500,000.00, has been deposited in the Department of Water Resources Electric Power Fund established in the State Treasury by Section 80200 of the California Water Code.

A representative of the California State Treasurer's Office hereby confirms the matters set forth in paragraph B.

Dated: June 26, 2001.

Authorized Representative, California Department of Water Resources

Representative
California State Treasurer's Office

AGENT RECEIPT

Morgan Guaranty Trust Company of New York ("MGT"), as agent for the Lenders under the Credit and Security Agreement dated as of June 26, 2001, among the State of California acting through the Department of Water Resources, various Lenders, and MGT, as Agent (the "Agreement"), hereby acknowledges (i) receipt of the amount of $193,500,000.00, constituting proceeds of $4,300,000,000 aggregate principal amount of Loans made on the date hereof by Lenders under the Agreement, which amount constitutes the Capitalized Interest and Fees Amount applicable to such Loans pursuant to the Agreement, and (ii) that such Capitalized Interest and Fees Amount has been deposited in the Interest and Fees Account established in the name of, and under the dominion and control of, MGT as agent for the Lenders pursuant to Section 2.11(c) of the Agreement.

Dated: June 26, 2001.

MORGAN GUARANTY TRUST
COMPANY OF NEW YORK, as Agent

By _____
Name:
Title:

CERTIFICATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES AS TO POWER SUPPLY AGREEMENTS

The California Department of Water Resources (the "Department") hereby certifies that the power supply agreements ("Power Supply Agreements") attached hereto have been executed pursuant to Division 27 (commencing with Section 80000) of the Water Code, are true and correct copies (as redacted in order to comply with certain confidentiality requirements contained therein, and are in full force and effect.

Neither the Credit and Security Agreement dated as of June 26, 2001, between the State of California acting through the Department, various Lenders and Morgan Guaranty Trust Company of New York, as Agent (the "Agreement"), nor the Department's Determination to Issue Bonds dated the date hereof (the "Determination"), nor any of the provisions thereof, constitute a breach of or default under any of the Power Supply Agreements.

Dated: June 26, 2001.

CALIFORNIA DEPARTMENT OF
WATER RESOURCES

By Perla Netto-Brown

Perla Netto-Brown
Chief of Fiscal Services

CALIFORNIA POWER EXCHANGE BLOCK FORWARD CONTRACTS

In February, 2001, under Executive Orders of the Governor, the State of California seized the existing block forward contracts of the California Power Exchange (the PX Block Forward Contracts). In it accounting for the contracts, DWR has treated these contracts, which are generally quarterly contracts, as a block of power for the period of February through December 2001. These are accounted for as two contracts in DWR's summary of its contracts; one group for delivery into NP 15 and one group for delivery into SP 15. There is not a contract for these individual PX Block Forward Contracts with DWR as a signatory. Enclosed is a list of those contracts, by counter party, showing the volume (MWh per hour), the price per MWh, and the term for the contracts. Please note that those block forwards which were for the first quarter of 2001 are shown as Feb-Mar 2001 because the State did not have possession of the contracts in the first month of those contracts. These are market deliveries for firm power during peak hours.

BLOCK FORWARDS - REASSIGNED FROM CALPX

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	CPSC	CONSTELLATION POWER SOURCE	25	$91.50	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$79.50	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$79.75	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$79.50	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$79.25	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	50	$76.00	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	50	$74.75	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$72.75	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$69.75	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$69.50	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$72.00	FEB-MAR 01	PEAK
	EPMI	ENRON POWER	50	$83.00	FEB-MAR 01	PEAK
	EPMI	ENRON POWER	50	$79.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	25	$78.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	50	$83.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	25	$78.50	FEB-MAR 01	PEAK
		TOTAL	525			
[redacted]	DETM	DUKE ENERGY	25	$75.75	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$75.10	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$58.00	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$71.20	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$73.25	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	25	$72.90	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	50	$67.05	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	50	$98.00	FEB-MAR 01	PEAK
	DETM	DUKE ENERGY	50	$46.00	FEB-MAR 01	PEAK
	EPMI	ENRON POWER	50	$46.50	FEB-MAR 01	PEAK
	SCEM	MIRANT	75	$47.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	50	$49.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	50	$46.00	FEB-MAR 01	PEAK
	SCEM	MIRANT	50	$46.25	FEB-MAR 01	PEAK
	SCEM	MIRANT	25	$75.25	FEB-MAR 01	PEAK
	PETP	PGET	25	$78.00	FEB-MAR 01	PEAK
		TOTAL	625			

BLOCK FORWARDS - REASSIGNED FROM CALPX

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	CPSC	CONSTELLATION POWER SOURCE	25	$62.00	Q2 2001	PEAK
	CPSC	CONSTELLATION POWER SOURCE	25	$62.00	Q2 2001	PEAK
	CPSC	CONSTELLATION POWER SOURCE	25	$63.00	Q2 2001	PEAK
	CPSC	CONSTELLATION POWER SOURCE	25	$59.50	Q2 2001	PEAK
	DETM	DUKE ENERGY	50	$65.00	Q2 2001	PEAK
	DETM	DUKE ENERGY	50	$64.25	Q2 2001	PEAK
	DETM	DUKE ENERGY	50	$60.00	Q2 2001	PEAK
	SCEM	MIRANT	25	$78.50	Q2 2001	PEAK
		TOTAL	275			
[redacted]	DETM	DUKE ENERGY	25	$75.75	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$75.10	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$71.20	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$73.25	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$72.90	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$69.25	Q2 2001	PEAK
	DETM	DUKE ENERGY	25	$69.50	Q2 2001	PEAK
	DETM	DUKE ENERGY	50	$56.00	Q2 2001	PEAK
	PETP	PGET	25	$78.00	Q2 2001	PEAK
	SCEM	MIRANT	75	$53.25	Q2 2001	PEAK
	SCEM	MIRANT	50	$53.00	Q2 2001	PEAK
	SCEM	MIRANT	50	$55.00	Q2 2001	PEAK
	SCEM	MIRANT	25	$75.25	Q2 2001	PEAK
	MERL	MERRILL LYNCH	50	$55.50	Q2 2001	PEAK
		TOTAL	500			

BLOCK FORWARDS - REASSIGNED FROM CALPX

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	CPSC	CONSTELLATION	50	$125.00	Q3 2001	PEAK
	CPSC	CONSTELLATION	50	$121.00	Q3 2001	PEAK
	CPSC	CONSTELLATION	50	$128.00	Q3 2001	PEAK
	CPSC	CONSTELLATION	-50	-$128.50	Q3 2001	PEAK
	CPSC	CONSTELLATION	50	$143.00	Q3 2001	PEAK
	CPSC	CONSTELLATION	25	$146.00	Q3 2001	PEAK
	DETM	DUKE	25	$79.25	Q3 2001	PEAK
	DETM	DUKE	75	$131.50	Q3 2001	PEAK
	DETM	DUKE	50	$124.00	Q3 2001	PEAK
	DETM	DUKE	50	$128.50	Q3 2001	PEAK
	DETM	DUKE	50	$128.75	Q3 2001	PEAK
	SCEM	MIRANT	25	$78.50	Q3 2001	PEAK
	SCEM	MIRANT	50	$127.00	Q3 2001	PEAK
		TOTAL	500			

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	CPSC	CONSTELLATION	25	$124.00	Q3 2001	PEAK
	DETM	DUKE	25	$75.75	Q3 2001	PEAK
	DETM	DUKE	25	$75.10	Q3 2001	PEAK
	DETM	DUKE	25	$71.20	Q3 2001	PEAK
	DETM	DUKE	25	$73.25	Q3 2001	PEAK
	DETM	DUKE	25	$72.90	Q3 2001	PEAK
	DETM	DUKE	25	$113.75	Q3 2001	PEAK
	DETM	DUKE	50	$125.00	Q3 2001	PEAK
	DETM	DUKE	50	$99.95	Q3 2001	PEAK
	EPMI	ENRON	250		Q3 2001	PEAK
	PETP	PGET	25	$114.00	Q3 2001	PEAK
	PETP	PGET	25	$78.00	Q3 2001	PEAK
	SCEM	MIRANT	75	$102.00	Q3 2001	PEAK
	SCEM	MIRANT	50	$95.00	Q3 2001	PEAK
	SCEM	MIRANT	50	$105.00	Q3 2001	PEAK
	SCEM	MIRANT	25	$75.25	Q3 2001	PEAK
	SCEM	MIRANT	50	$99.75	Q3 2001	PEAK
	SCEM	MIRANT	50	$127.00	Q3 2001	PEAK
	SCEM	MIRANT	50	$107.00	Q3 2001	PEAK
		TOTAL	925			

BLOCK FORWARDS - REASSIGNED FROM CALPX

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	DETM	DUKE	50	$67.25	Q4 2001	PEAK
	DETM	DUKE	50	$67.25	Q4 2001	PEAK
NP15	SCEM	MIRANT	25	$78.50	Q4 2001	PEAK
		TOTAL	125			

Path	Scheduling Coordinator	Counter-Party	Volume in MWh	Price	Term	Delivery Period
[redacted]	DETM	DUKE	25	$75.75	Q4 2001	PEAK
	DETM	DUKE	25	$75.10	Q4 2001	PEAK
	DETM	DUKE	25	$71.20	Q4 2001	PEAK
	DETM	DUKE	25	$73.25	Q4 2001	PEAK
	DETM	DUKE	25	$72.90	Q4 2001	PEAK
	DETM	DUKE	50	$42.00	Q4 2001	PEAK
	EPMI	ENRON	50		Q4 2001	PEAK
	PETP	PGET	25	$78.00	Q4 2001	PEAK
	SCEM	MIRANT	25	$75.25	Q4 2001	PEAK
	SCEM	MIRANT	50	$42.00	Q4 2001	PEAK
	SCEM	MIRANT	50	$41.00	Q4 2001	PEAK
	SCEM	MIRANT	75	$41.00	Q4 2001	PEAK
		TOTAL	450			

Documents Enclosed in June 15, 2001 CDWR Document Production

Contracts with the following counterparties:

Allegheny Energy Supply Company	3
Alliance Colton LLC	1
Bonneville Power Administration	2
Calpine Energy Services, L.P.	3
Constellation Power Source, Inc.	1
Coral Power, L.L.C.	4
Dynegy Power Marketing, Inc.	6
El Paso Merchant Energy, L.P.	2
GWF Energy LLC	1
High Desert Power Project, LLC	1
Mirant Americas Energy Marketing	1
Morgan Stanley Capital Group Inc.	1
PG&E Energy Trading – Power, L.P.	1
Pinnacle West Capital Corporation	2
Primary Power (Imperial Valley Resource Recovery Company, L.L.C.)	1
Sempra Energy Resources	2
Soledad Energy, LLC	1
Williams Energy Marketing & Trading Company	4
California Power Exchange Block Forward Contracts	

CDWR version of EEI Master Power Purchase & Sale Agreement

Western Systems Power Pool Agreement

DEPARTMENT OF WATER RESOURCES

CALIFORNIA ENERGY RESOURCES SCHEDULING

LONG TERM ENERGY CONTRACTS

JUNE 15, 2001

Documents Enclosed in June 15, 2001 CDWR Document Production

Contracts with the following counterparties:

Allegheny Energy Supply Company

Alliance Colton LLC

Bonneville Power Administration

Calpine Energy Services, L.P.

Constellation Power Source, Inc.

Coral Power, L.L.C.

Dynegy Power Marketing, Inc.

El Paso Merchant Energy, L.P.

GWF Energy LLC

High Desert Power Project, LLC

Mirant Americas Energy Marketing

Morgan Stanley Capital Group Inc.

PG&E Energy Trading – Power, L.P.

Pinnacle West Capital Corporation

Primary Power (Imperial Valley Resource Recovery Company, L.L.C.)

Sempra Energy Resources

Soledad Energy, LLC

Williams Energy Marketing & Trading Company

CDWR version of EEI Master Power Purchase & Sale Agreement

Western Systems Power Pool Agreement

Power Supply Agreements Not Included

No Litigation Certificate of the Attorney General

I, BILL LOCKYER, Attorney General of the State of California, hereby certify, with respect to execution and delivery by the State of California Department of Water Resources ("Department") of a Credit and Security Agreement ("Agreement") dated as of June 26, 2001, among the State of California by and through the Department, various lenders and Morgan Guaranty Trust Company of New York, as Agent, that, to the best of my knowledge, except as set forth on Schedule 3 thereto, there is no action, suit, proceeding, inquiry or investigation at law or in equity before or by any court, arbitrator, or governmental entity pending, with service of process completed on the State, California Public Utility Commission (CPUC) or the Department, or threatened against the State, the CPUC or the Department, which

(a) challenges the constitutionality, validity or enforceability of any of the Transaction Documents or the pledge of or lien on the Collateral contained therein;

(b) challenges the existence, organization or powers of the State, the Department, the CPUC or any elected or appointed official thereof to adopt, execute and deliver any of the Transaction Documents or perform the obligations thereunder or contemplated thereby; or

(c) challenges the constitutionality or validity of AB1X or Division 27 of the Water Code the Emergency Proclamation, the Executive Order or the powers of the State, the Department, or the CPUC thereunder, including without limitation the power to purchase and sell electric power, to borrow money to purchase electric power or natural gas for the generation of electric power, to collect payment for such electric power or to establish a revenue requirement as defined or the constitutionality or validity of the Emergency Services Act or the Governor's powers thereunder.

In making this certificate, the undersigned has not performed a docket search of federal and state court filings. The undersigned has contacted the CPUC legal office, including the Commission President's Legal Advisor, for the purpose of identifying relevant decisions and filings and has inquired of senior legal staff and executive staff within the Attorney General's Office responsible for coordinating and managing judicial and administrative actions impacting the Governor's Emergency Proclamation, the Executive Order or AB1X and its implementation.

Capitalized terms not defined herein shall have the meanings assigned thereto in the Agreement.

IN WITNESS WHEREOF, I have executed this certificate this 26 day of June, 2001.

Catherine Van Aken

CATHERINE VAN AKEN
Supervising Deputy Attorney General

For BILL LOCKYER
Attorney General

BILL LOCKYER
Attorney General

State of California
DEPARTMENT OF JUSTICE

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June 26, 2001

California Department of Water Resources
The Lenders under the Credit and Security Agreement
Morgan Guaranty Trust Company of New York, as Agent

RE: Credit and Security Agreement Dated June 26, 2001

Ladies and Gentlemen:

We have acted as the Attorney General of the State of California in connection with execution and delivery of the Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement"), among the Department of Water Resources (the "Department") and the lenders thereunder and the bonds being issued thereunder (the "Bonds"). The Credit Agreement has been executed and delivered by the Department pursuant to Division 27 of the California Water Code, Chapter 7 of Division 1 of Title 2 of the California Government Code and the Executive Order by the Governor of the State of California, dated June 18, 2001 (the "Order"). Capitalized terms used herein have the meanings given to such terms in the Credit Agreement.

In such connection, we have reviewed the Order (and prior Executive Orders and Proclamations related to the state of emergency due to shortages of electricity in the State), the Credit Agreement, the Bonds, the written Determination to issue bonds executed by the Director of the Department (the "Determination"), the Certificate of the Department dated the date hereof and relating to the Credit Agreement and describing the historical scope of the duties of the Department (the "Certificate") and other certificates, documents and matters to the extent we deemed necessary to render the opinions set forth herein. We have assumed, without undertaking to verify, the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the Department. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents referred to in this paragraph.

The opinions and conclusions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions and conclusions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof and we disclaim any obligation to update this letter. Except as expressly set forth below, we express no opinion with respect to any indemnification, contribution, penalty, choice of forum or waiver provisions contained in the documents described herein. In addition, we call attention to the fact that the rights and obligations under the Credit Agreement and their enforceability may be subject to bankruptcy, insolvency, reorganization, fraudulent conveyance, arrangement, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to procedural limitations on legal remedies against the State or a public agency of the State, including those referenced in California Code of Civil Procedure sections 695.040, 695.050 and 712.070 and California Government Code sections 900 through 985.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Department is a department of the State of California, duly established and validly existing under the laws of the State of California.

2. The Credit Agreement has been duly authorized, executed and delivered by the Department, and constitutes the valid and binding agreement of the Department, enforceable in accordance with its terms.

3. The Credit Agreement creates a valid pledge of Water Code Collateral, including the Revenues, that it purports to create. Pursuant to Division 27 of the Water Code, the pledge of Revenues and other Collateral made by the Department in the Credit Agreement is valid, binding and perfected without any physical delivery, recordation, filing or further act, and the lien thereof is valid, binding and perfected.

4. The Bonds constitute valid and binding limited Obligations of the Department payable in accordance with the Credit Agreement. Neither the Obligations under the Credit Agreement nor the Bonds constitute a debt or liability of the State or of any political subdivision thereof, nor constitute a general obligation of the Department. Neither the faith and credit nor the taxing power of the State or of any political subdivision thereof is pledged to the payment of the principal of,

premium, if any, or interest on the Bonds or any Obligation under the Credit Agreement. The Department has no taxing power.

This letter is delivered to you solely for your benefit, and is not to be used, circulated, quoted or otherwise referred to or relied upon for any other purpose or by any other person. By acceptance of this letter, the Agent and Lenders recognize and acknowledge that no attorney-client relationship has existed between this Office and the Agent or Lenders in connection with the Credit Agreement or by virtue of this letter. This opinion is limited to the laws of the State of California.

Sincerely,

Pamela Smith-Steward

PAMELA SMITH-STEWARD
Chief Assistant Attorney General

For BILL LOCKYER
Attorney General

I:\Gvt\Public Finance Bonds - Energy Bond Opinions\Validity Opinion Bridge Loan.wpd

BILL LOCKYER
Attorney General

State of California
DEPARTMENT OF JUSTICE

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June 26, 2001

California Department of Water Resources
The Lenders under the Credit and Security Agreement
Morgan Guaranty Trust Company of New York, as Agent

RE: No Merit Opinion – *Howard Jarvis Taxpayers Association, et al v. Kathleen Connell*

Ladies and Gentlemen:

You have asked for our opinion regarding the impact of the above-captioned lawsuit, if any, on the validity of the appropriation provided by Section 80200 of the California Water Code. Section 80200 provides that all the moneys in the Department of Water Resources Electric Power Fund are continuously appropriated, without regard to fiscal year, to the Department of Water Resources, and shall be available for the purposes of Division 27 of the Water Code.

BACKGROUND

The relevant background facts are as follows:

On June 24, 1998, the Howard Jarvis Taxpayers Association and other plaintiffs filed a complaint in the Los Angeles County Superior Court for certain declaratory and injunctive relief, naming the Controller of the State of California as defendant in the matter of *Howard Jarvis Taxpayers Association, et al v. Kathleen Connell*. The Attorney General represented the Controller in these proceedings. On July 21, 1998, after hearing oral arguments, the Superior Court issued a preliminary injunction that prohibited the Controller from making any payments pursuant to any continuing appropriation. This would include the continuous appropriation in Section 80200 of the California Water Code.

On July 28, 1998 (modified on July 29), in response to a petition from certain intervenors in the case, the California Court of Appeal, Second Appellate District, issued an order granting a Writ of Supersedes, resulting in a stay of the Superior Court's preliminary injunction, pending a Court of Appeal decision on the merits of the matter. On July 22, 1998, the Attorney General

filed on behalf of the Controller, in the California Supreme Court, a request for immediate stay and petition for writ of mandate, prohibition or other appropriate relief, naming the Superior Court as respondent and Howard Jarvis Taxpayers Association and others as real parties in interest. The petition asked the Supreme Court to vacate the order of the Superior Court and provide other relief. On July 29, 1998, the Supreme Court, noting the issuance of the writ by the Court of Appeal, transferred the Controller's petition to the Court of Appeal, where it has been consolidated with the other action. The case is now pending before the Court of Appeal. Briefs have been submitted, but no date has yet been set for oral argument.

DISCUSSION

Subsequent to the actions described in the preceding two paragraphs, Budget Acts have been enacted, but the *Jarvis* case remains on appeal in the Court of Appeal.

The Superior Court's injunction was apparently based on its interpretation of Article IV, Section 12, of the California Constitution which reads, in relevant part, as follows:

> "(c). . . Until the budget bill has been enacted, the Legislature shall not send to the Governor for consideration any bill appropriating funds for expenditure during the fiscal year for which the budget bill is to be enacted, except emergency bills recommended by the Governor or appropriations for the salaries and expenses of the Legislature.
>
> (d) No bill except the budget bill may contain more than one item of appropriation, and that for one certain, expressed purpose."

The Superior Court's memorandum of decision, supporting its order, states in part as follows:

> ". . . The so-called 'continuing appropriations' have no constitutional base and simply represent examples of expenditures from the State Treasury that have no unique position over other required expenditures. . . . Each of the examples argued by defendant as allowing the issuance of warrants without the enactment of a budget bill and legislature appropriation do not present exceptions to the prohibition of Article IV, Section 12(c). To allow such an interpretation would render Article IV, Section 12(c), an ineffective goal and not, as it is, a constitutional mandate.

In connection with the rendering of this opinion, we have reviewed the legal pleadings in the *Jarvis* case and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. The opinions expressed herein are based on an analysis of existing laws and court decisions and cover certain matters not directly addressed by such authorities.

Based on our review of the legal pleadings and of the appropriate legal authorities and in reliance thereon, as of the date hereof, we are of the opinion that the Superior Court's conclusion in *Jarvis* questioning the validity of continuing appropriations, if and to the extent it would apply to Section 80200 of the California Water Code is without merit, and that the California appellate courts would so hold.

This letter is delivered to you solely for your benefit and is not to be used, circulated, quoted or otherwise referred to or relied upon for any other purpose or by any other person, other than as expressly approved by us. No attorney-client relationship has existed or exists between us and the Lenders or the Agent in connection with the matters covered by this letter or by virtue of this letter.

Sincerely,

Catherine Van Aken

CATHERINE VAN AKEN
Supervising Deputy Attorney General

For BILL LOCKYER
Attorney General

BILL LOCKYER
Attorney General

State of California
DEPARTMENT OF JUSTICE

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June 26, 2001

California Department of Water Resources
The Lenders under the Credit and Security Agreement
Morgan Guaranty Trust Company of New York, as Agent

RE: No Merit Opinion - *Hendricks v. Hannigan*

Ladies and Gentlemen:

You have asked for our opinion regarding a case entitled *Ruth Hendricks* v. *Thomas M. Hannigan, Director of the California State Department of Water Resources*, San Diego Superior Court Number GIC761051, which was filed on January 19, 2001. This case challenges the legality of the Department of Water Resources' use of general funds appropriated pursuant to Senate Bill 7X to purchase electrical power from certain named power providers and make that power available to Pacific Gas and Electric and Southern California Edison.

In connection with the rendering of this opinion, we have reviewed the complaint filed on January 19, 2001, in the above-referenced case, and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. The opinions expressed herein are based on an analysis of existing laws and court decisions and cover certain matters not directly addressed by such authorities.

Based upon our review of the complaint and of the appropriate legal authorities and in reliance thereon, as of the date hereof, we are of the opinion that the allegations of the complaint are without merit.

This opinion is limited to the matters expressly set forth herein, and no opinion is implied or may be inferred beyond the matters expressly stated herein. This letter is delivered to you solely for your benefit and is not to be used, circulated, quoted or otherwise referred to or relied upon for any other purpose or by any other person, other than as expressly approved by us. No

attorney-client relationship has existed or exists between us and the Lenders or the Agent in connection with the matters covered by this letter or by virtue of this letter.

Sincerely,

Catherine Van Aken

CATHERINE VAN AKEN
Supervising Deputy Attorney General

For BILL LOCKYER
Attorney General

STATE OF CALIFORNIA -- THE RESOURCES AGENCY GRAY DAVIS, *Governor*

DEPARTMENT OF WATER RESOURCES
1416 NINTH STREET, P.O. BOX 942836
SACRAMENTO, CA 94236-0001
(916) 653-5791

June 26, 2001

The Agent and Lenders under the
Credit and Security Agreement
described below
c/o Morgan Guaranty Trust Company
of New York, as Agent

Credit and Security Agreement - Dated June 26, 2001

I am Chief Counsel of the Department of Water Resources of the State of California (the "Department") and am delivering this opinion in connection with execution and delivery of the Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement"), between you and the Department, and the Bonds being issued thereunder. The Credit Agreement has been executed and delivered by the Department pursuant to Division 27 of the California Water Code (the "Electric Power Act"), Chapter 7 of Division 1 of Title 2 of the California Government Code (the "Emergency Services Act") and the Executive Order by the Governor of the State of California, dated June 18, 2001 (the "Order"). Capitalized terms used herein have the meanings given to such terms in the Credit Agreement.

In such connection, I have reviewed the Order, the Credit Agreement, the Bonds, the Certificate of the Department dated the date hereof and relating to the Credit Agreement and such other documents, opinions and matters to the extent I deemed necessary to render the opinions set forth herein. I have assumed, without undertaking to verify, the due and legal execution thereof by, and the validity thereof against, any parties other than the Department.

The opinions and conclusions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions and conclusions may be affected by actions taken or omitted or events occurring after the date hereof. I have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to my attention after the date hereof and I disclaim any obligation to update this letter. Except as expressly set forth below, I express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum or waiver provisions contained in the documents described herein. In addition, I call attention to the fact that the rights and obligations under the Credit Agreement and the Transaction Documents and their enforceability may be subject to bankruptcy, insolvency, reorganization, fraudulent conveyance, arrangement, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against the State of California, including

those referenced in California Code of Civil Procedure Sections 695.040, 695.050 and 712.070 and California Government Code Sections 900 through 985.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, I am of the following opinions:

1. The Department (i) is a department of the State of California, duly established and validly existing under the laws of the State of California, (ii) has all requisite power and authority to authorize, execute, deliver and perform all of its obligations under the Credit Agreement and the other Transaction Documents, to incur the Obligations, to authorize, execute and deliver any and all instruments and documents required to be authorized, executed or delivered pursuant to or in connection herewith or therewith, and to perform each and all of the matters and things provided for herein and therein, and (iii) has all requisite authorizations, orders, consents, approvals, licenses, exemptions from or registrations with any Governmental Authority necessary for the valid execution, delivery and performance by the Department of any of the Transaction Documents.

2. The execution, delivery and performance by the Department of this Agreement and the other Transaction Documents and any and all instruments or documents required to be executed or delivered in connection herewith or therewith have been duly authorized and do not and will not (i) violate any provision of the Constitution of the State or the United States, any law, rule, regulation, order, writ, judgment, injunction, decree, determination or award in effect having applicability to the Department or (ii) result in a breach of or constitute a default under any indenture, loan, credit agreement or any other agreement, lease or instrument to which the Department is a party or by which the Department is bound which could reasonably be expected to adversely affect the Department's ability to satisfy and perform its obligations under the Transaction Documents.

3. The Credit Agreement and each Transaction Document have been duly authorized, executed and delivered by the Department.

4. Except as set forth in Schedule 3 to the Credit Agreement, there is no action, suit, proceeding, inquiry or investigation at law or in equity before or by any arbitrator, Governmental Authority, pending with service made or, to the best knowledge of the Department, threatened against or affecting the Department, which (a) in any manner draws into question the constitutionality, validity or enforceability of any of the Transaction Documents or the pledge of or lien over the Collateral, (b) in any way contests the existence, organization or powers of the Department or any elected or appointed official thereof to adopt, execute and deliver any of the Transaction Documents or perform the obligations thereunder or contemplated thereby, or (c) in any way contests the constitutionality or validity of the Electric Power Act, the Emergency Services Act or the Order or the powers of the State or the Department thereunder, including without limitation the power of the Department to purchase and sell electric

power and collect payment for such electric power or to establish a revenue requirement.

This opinion is delivered to you solely for your benefit and is not to be used, circulated, quoted or otherwise referred to or relied upon for any other purpose or by any other person. This opinion is limited to the laws of the State of California and the federal laws of the United States of America.

Sincerely,

for Susan Weber
Chief Counsel

ORRICK, HERRINGTON & SUTCLIFFE LLP
OLD FEDERAL RESERVE BANK BUILDING
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June 26, 2001

The Agent and Lenders under the
Credit and Security Agreement
described below
c/o Morgan Guaranty Trust Company of New York,
as Agent

Re: Credit and Security Agreement,
dated June 26, 2001

Ladies and Gentlemen:

We have acted as special counsel to the Department of Water Resources of the State of California (the "Department") and are delivering this opinion in connection with execution and delivery of the Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement"), between you and the Department, and the Bonds being issued thereunder. The Credit Agreement has been executed and delivered by the Department pursuant to Division 27 of the California Water Code, Chapter 7 of Division 1 of Title 2 of the California Government Code and the Executive Order by the Governor of the State of California, dated June 26, 2001 (the "Order"). Capitalized terms used herein have the meanings given to such terms in the Credit Agreement.

In such connection, we have reviewed the Order, the Credit Agreement, the Bonds, the Certificate of the Department dated the date hereof and relating to the Credit Agreement and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein. We have assumed, without undertaking to verify, the due and legal execution thereof by, and the validity thereof against, any parties other than the Department.

The opinions and conclusions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions and conclusions may be effected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof and we disclaim any obligation to update this letter. Except as expressly set forth below, we express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum or waiver provisions contained in the

documents described herein. In addition, we call attention to the fact that the rights and obligations under the Credit Agreement and their enforceability may be subject to bankruptcy, insolvency, reorganization, fraudulent conveyance, arrangement, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against the State of California, including those referenced in California Code of Civil Procedure Sections 695.040, 695.050 and 712.070 and California Government Code Sections 900 through 985.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Department (i) is a department of the State of California, duly established and validly existing under the laws of the State of California, and (ii) has all requisite power and authority to authorize, execute, deliver and perform all of its obligations under the Credit Agreement, to incur the Obligations, to authorize, execute and deliver any and all instruments and documents required to be authorized, executed or delivered pursuant to or in connection therewith, and to perform each and all of the matters and things provided for therein.

2. The Credit Agreement has been duly authorized, executed and delivered by the Department, and constitutes the valid and binding agreement of the Department, enforceable in accordance with its terms.

This letter is furnished by us as special counsel to the Department, is delivered to you solely for your benefit, and is not to be used, circulated, quoted or otherwise referred to or relied upon for any other purpose or by any other person. By acceptance of this letter you recognize and acknowledge that no attorney-client relationship has existed between our firm and yourselves in connection with the Credit Agreement or by virtue of this letter. This opinion is limited to the laws of the State of California and the federal laws of the United States of America.

Very truly yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP

per Stanley J. Dirks

Hawkins, Delafield & Wood
633 West Fifth Street
Suite 3550
Los Angeles, California 90071

June 26, 2001

California Department of Water Resources
The Lenders under the Credit and Security Agreement
Morgan Guaranty Trust Company of New York, as Agent

Ladies and Gentlemen:

We have acted as bond counsel in connection with the execution and delivery by the State of California Department of Water Resources (the "Department") of a Credit and Security Agreement (the "Agreement") dated as of June 26, 2001, among the State of California (the "State"), acting through the Department, the Lenders thereunder and Morgan Guaranty Trust Company of New York, as Agent, pursuant to the Constitution and laws of the State, including the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code, the "Emergency Services Act"); a Proclamation of the State Governor dated January 17, 2001, issued pursuant to the Emergency Services Act, concerning the state of emergency due to shortages of electricity available in the State (the "Proclamation"); Division 27 (commencing with Section 80000) of the California Water Code, added by Chapter 4 of the Statutes of 2001 (Assembly Bill No. 1 of the First Extraordinary Session of 2001) ("AB1X"), as amended (the "Act"); and Executive Order D-42-01 of the State Governor dated June 18, 2001 (the "Order"); and the written Determination to issue Bonds dated the date hereof, executed by the Director of the Department (the "Determination"); and, collectively with the Emergency Services Act, the Proclamation, the Act, the Order and the Determination, the "Enabling Authorization"). Capitalized terms used but not defined herein shall have the respective meanings ascribed thereto in the Agreement.

The Agreement provides for the execution and delivery by the Department of Bonds on the terms and conditions specified in the Agreement. The Bonds have been executed and delivered for the purpose of providing the Department with funds to purchase electric power, to purchase natural gas for use in the generation of electric power to be purchased by the Department, and to pay costs related thereto and other costs as provided in the Order. The Bonds and are payable and secured as set forth in the Agreement. The Department is permitted under the Agreement to issue Parity Debt only on the terms and conditions set forth in the Agreement.

The Act provides for, among other things, the following: the authority of the Department to contract with any person, local publicly owned electric utility, or other entity for the purchase of power on such terms and for such periods as the Department determines and at such prices as the Department deems appropriate, and upon those terms, limitations, and conditions as it prescribes; the authority of the Department to incur indebtedness and issue bonds, notes and other evidences of indebtedness, and to provide for their payment and security, as prescribed therein; and the authority of the Department to contract with electrical corporations to

transmit or provide for the transmission of, and distribute the power and provide billing, collection, and other related services, as agent of the Department, on terms and conditions that reasonably compensate the electrical corporations for their services. The Act also provides that the Department shall retain title to all power sold by it to the retail end use customers and that upon the delivery of power to them, the retail end use customers shall be deemed to have purchased that power from the Department. The Act provides that, for purposes of the Act and except as otherwise provided in the Act, the authority of the California Public Utilities Commission (the "Commission") as set forth in Section 451 of the California Public Utilities Code shall apply, except that any just and reasonable review under that Section is to be conducted and determined by the Department. The Act provides that the Department shall be entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to comply with Section 80134 of the California Water Code. Section 80134 provides that the Department shall notify the Commission of its revenue requirements and provides that such revenue requirements shall include, among other things, amounts necessary to pay principal of and interest on all of its bonds as and when due, amounts necessary to pay for power purchased by it and other related expenses, the Department's administrative costs and repayment of advances.

The Order provides, among other things, for the Department to accept loans on behalf of the Governor as more particularly described therein.

We have examined a record of proceedings relating to the execution and delivery by the Department of the Agreement and the execution and delivery of the Bonds, and based on the foregoing and our examination of existing law, such legal proceedings and such other documents as we deem necessary to render this opinion, we are of the opinion that:

1. (A) The Department is duly existing under the laws of the State, and is validly authorized under the laws of the State, particularly the Enabling Authorization, to execute and deliver the Agreement and the Bonds. The Agreement and the Bonds have been duly authorized, executed and delivered by the Department and constitute valid and binding agreements of the Department, enforceable against the Department in accordance with their terms. The Bonds constitute valid and binding limited special obligations of the Department payable from the Collateral, including the Revenues pledged and the other collateral provided therefor in the Agreement. The Bonds do not constitute a debt or liability of the State or of any political subdivision thereof, and do not constitute a general obligation of the Department. Neither the faith and credit nor the taxing power of the State or of any political subdivision thereof is pledged to the payment of the principal of, premium, if any, or interest on the Bonds. The Department has no taxing power.

(B) Under the laws of the State, including the State Constitution, and under the Constitution of the United States, AB1X was duly adopted as an urgency statute pursuant to Article IV, Section 8, of the State Constitution, does not change the duties of any office within the meaning of that provision, and is valid with respect to all provisions thereof material to the subject matter of this opinion letter. Section 8(d) of Article IV of the State Constitution defines urgency statutes and the circumstances under which they may be adopted, and provides in part as follows: "An urgency statute may not create or abolish any office or change the salary, term, or duties of any office, or grant any franchise or special privilege, or create any vested right or interest." In rendering the opinion expressed in this paragraph, we have relied on a certificate dated the date hereof, executed by the Director of the Department, relating to the historical scope of the duties of the Department.

(C) The Order is valid.

2. The Enabling Authorization validly provides that the Department shall be entitled to recover its revenue requirements, and validly provides for the payment to the Department of Revenues from the ratepayers and for the enforcement of payment, if necessary, by the Department, all in accordance with the Enabling Authorization. The Department has validly covenanted in the Agreement to establish and revise Revenue Requirements which, after taking into account certain other funds, shall be at least sufficient to pay its Operating and Maintenance Costs and principal of and interest on the Bonds.

3. The Agreement creates the valid pledge of Water Code Collateral, including the Revenues, that it purports to create. The lien of this pledge for the security of the Agreement and the Bonds is and, pursuant to covenants of the Department in the Agreement, will be prior to all other liens thereon, subject only to the provisions of the Agreement permitting the payment or use of the Revenues and other Water Code Collateral for the purposes (including the payment of Operating and Maintenance Costs), in the manner and upon the terms and conditions set forth in the Agreement. Pursuant to the Act, the pledge of Revenues and other Collateral made by the Department in the Agreement is valid, binding and perfected without any physical delivery, recordation, filing or further act, and the lien thereof is valid, binding and perfected against all parties having claims of any kind in tort, contract or otherwise against the Department irrespective of whether such parties have notice thereof.

4. No registration with, consent of, or approval by any governmental agency or commission that has not been obtained is necessary for the execution and delivery of the Agreement or the Bonds.

5. The Department has validly included in the Agreement and the Bonds the pledge and undertaking of the State that so long as any obligations of the Department incurred under the Agreement or the other Transaction Documents remain outstanding and not fully performed or discharged, the rights, powers, duties and existence of the Department and the California Public Utilities Commission shall not be diminished or impaired in any manner that will adversely affect the interests and rights of the Agent or any Lender.

6. Pursuant to the Act, interest on the Tax-Exempt Bonds and Taxable Bonds is exempt from personal income taxes imposed by the State of California.

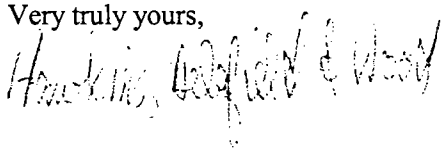
7. Under existing statutes and court decisions, interest on the Tax-Exempt Bonds is not included in gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Tax Code of 1986, as amended (the "Tax Code"). Under the Tax Code, interest on the Tax-Exempt Bonds is not treated as a preference item in calculating alternative minimum taxable income for purposes of the alternative minimum tax applicable to individuals and corporations; such interest, however, is includable in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations by the Tax Code. In rendering the opinions in this paragraph 7, we have relied upon and assumed (i) the material accuracy of the representations, statements of intention and reasonable expectations, and certifications of fact, contained in the Tax Certificate delivered on the date hereof by the Department with respect to the use of proceeds of the Tax-Exempt Bonds and the investment of certain funds, and other matters affecting the non-inclusion of interest on the Tax-Exempt Bonds in gross income for Federal income tax purposes under Section 103 of the Tax Code, and (ii) compliance by the Department with procedures and covenants set forth in the Tax Certificate and with the tax covenants set forth in the Agreement and other Transaction Documents as to such matters. Under the Tax Code, failure to comply with such procedures and covenants may cause the interest on the Tax-Exempt Bonds to be included in gross income for Federal income tax purposes, retroactive to the date of issuance of the Tax-Exempt Bonds, irrespective of the date on which such noncompliance occurs or is ascertained.

Except as stated in paragraphs 6 and 7 above, we express no opinion as to any Federal, State or local tax consequences arising with respect to the Tax-Exempt Bonds or the ownership or disposition thereof. Furthermore, we express no opinion as to the effect of any action hereafter taken or not taken in reliance upon an opinion of counsel other than ourselves on the exclusion from gross income for Federal income tax purposes of interest on the Tax-Exempt Bonds, or under State and local tax law.

We call attention to the fact that the enforceability of rights and remedies with respect to the Bonds and the Agreement may be limited by, and may be subject to: bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to generally applicable limitations on legal remedies against the State. We refer you to our supplemental opinion dated the date hereof as to certain Federal bankruptcy matters. We express no opinion with respect to any indemnification, contribution, choice of law, choice of forum or waiver provisions contained in the foregoing documents.

This opinion is issued as of the date hereof, and we assume no obligation to update, revise or supplement this opinion to reflect any action hereafter taken or not taken, or any facts or circumstances, or any changes in law or in interpretations thereof, that may hereafter arise or occur, or for any other reason.

Very truly yours,



Hawkins, Delafield & Wood
633 West Fifth Street
Suite 3550
Los Angeles, California 90071

June 26, 2001

California Department of Water Resources
Sacramento, California

Re: *Analysis of California Water Code §80200(a) and California Constitution Art. IV, §12*

Ladies and Gentlemen:

We are bond counsel to the State of California Department of Water Resources (the "Department") in connection with the execution and delivery by the Department of a Credit and Security Agreement (the "Agreement") dated as of June 26, 2001, among the State of California (the "State"), acting through the Department, the lenders thereunder and Morgan Guaranty Trust Company of New York, as Agent. The Agreement was entered into in accordance with and pursuant to the Constitution and laws of the State, including the Emergency Services Act, the Proclamation, the Act, the Emergency Regulations, the Determination, and the Certificate (all as defined in the Agreement and collectively referred to herein as the "Enabling Authorization"). The Agreement provides for the execution and delivery by the Department of Bonds (as defined in the Agreement) on the terms and conditions specified therein. Capitalized terms used herein and not otherwise defined shall have the meanings given to such terms in the Agreement.

The obligations of the Department under the Agreement and the Bonds are secured by continuing appropriations made pursuant to Water Code §80200(a) (the "Appropriations Statute"). You have requested our opinion regarding the validity of the Appropriations Statute in light of the restrictions upon spending and appropriations found in California Constitution Art. IV, §12.[1]

Caveats

The views expressed in this letter are not a guarantee of any particular outcome. Rather, they reflect only our informed professional judgment on the specific issues addressed herein. Litigation always involves inherent uncertainties and no outcome in any particular case can ever be predicted with complete accuracy. In this case, we have found no California authority which we consider to be binding on all of

[1]Section 80200(a) states:

There is hereby established in the State Treasury the Department of Water Resources Electric Power Fund. Notwithstanding Section 13340 of the Government Code, all moneys in the fund are continuously appropriated, without regard to fiscal year, to the department, and shall be available for the purposes of this division. It is the intent of the Legislature that this fund be a continuation of the fund created in Chapter 3 of the Statutes of 2001 (SB 7 of the First 2001-02 Extraordinary Session).

the issues discussed herein. However, as discussed below, there are authorities which we believe are persuasive and support our views. This opinion is also based upon proper presentation of this matter to the California appellate courts and the consistent application by such courts of the principles enunciated in prior California decisions.

Facts

The Howard Jarvis Taxpayers Association (the "Association") has instituted currently pending litigation against the State Controller in which it has argued that continuing appropriations are in violation of Article IV, §12 of the California Constitution and thus invalid. On July 21, 1998, after hearing oral arguments, the Superior Court in *Howard Jarvis Taxpayers Association, et al. v. Connell* issued a preliminary injunction prohibiting the State Controller from making any payments pursuant to any continuing appropriation.

The Superior Court reasoned simply that no budget bill had been passed for that fiscal year and the California Constitution prohibited (with only a few non-applicable exceptions) "appropriation bills without first having a budget bill enacted." Continuing appropriations bills were no exception. The Superior Court held:

> The so-called "continuing appropriations" have no constitutional base and simply represent examples of expenditures from the state treasury that have no unique position over other required expenditures....To allow such an interpretation would render Article IV, §12(c), an ineffective goal and not, as it is, a constitutional mandate.

This order has been stayed and awaits further proceedings in the appellate courts.

Analysis

Article IV, §12 of the California Constitution provides as follows:

> (a) Within the first 10 days of each calendar year, the Governor shall submit to the Legislature, with an explanatory message, a budget for the ensuing fiscal year containing itemized statements for recommended state expenditures and estimated state revenues. If recommended expenditures exceed estimated revenues, the Governor shall recommend the sources from which the additional revenues should be provided.
>
> (b) The Governor and the Governor-elect may require a state agency, officer or employee to furnish whatever information is deemed necessary to prepare the budget.
>
> (c) The budget shall be accompanied by a budget bill itemizing recommended expenditures. The bill shall be introduced immediately in each house by the persons chairing the committees that consider appropriations. The Legislature shall pass the budget bill by midnight on June 15 of each year. Until the budget bill has been enacted, the Legislature shall not send to the Governor for consideration any bill appropriating funds for expenditure during the fiscal year for which the budget bill is to be enacted, except emergency bills recommended by the Governor or appropriations for the salaries and expenses of the Legislature.
>
> (d) No bill except the budget bill may contain more than one item of appropriation, and that for one certain, expressed purpose. Appropriations from the

> General Fund of the State, except appropriations for the public schools, are void unless passed in each house by a rollcall vote entered in the journal, two-thirds of the membership concurring.
>
> (e) The Legislature may control the submission, approval, and enforcement of budgets and the filing of the claims for all State agencies.

Two major questions regarding Article IV, §12 and the *Jarvis* litigation require analysis. First, does the continuing appropriation made by the Appropriations Statute violate Article IV, §12 either because it is inconsistent with the express provisions of Article IV, §12, or because the budget is the exclusive means for the Legislature to appropriate money? Second, does the Appropriations Statute violate Article IV, §12(d) by containing more than one item of appropriation for one certain, expressed purpose? California precedents answer both of these questions in the negative.

The language now contained in Article IV, §12(c) of the California Constitution comes from similar language added to Article IV, §34 of the Constitution by amendment in 1922 to Article IV, §34 of the Constitution. After the 1922 amendments, Article IV, §34 stated:

> The Governor shall, within the first thirty days of each regular session of the Legislature and prior to its recess, submit to the Legislature, with an explanatory message, a budget containing a complete plan and itemized statement of all proposed expenditures of the state provided by existing law or recommended by him.... The budget shall be accompanied by an appropriation bill covering the proposed expenditures to be known as the budget bill. The budget bill shall be introduced immediately into each house of the Legislature by the respective chairmen of the committees having to do with appropriations.... Until the budget bill has been finally enacted, neither house shall place upon final passage any other appropriation bill, except emergency bills recommended by the Governor, or appropriations for the salaries, mileage, and expenses of the Senate and Assembly. No bill making an appropriation of money, except the budget bill, shall contain more than one item of appropriation, and that for one single and certain purpose to be therein expressed.... In case of conflict between this section and any other portion of this constitution, the provisions of this section shall govern, except that any item of appropriation in the Budget Act, other than for the usual current expenses of the state, shall be subject to the referendum.

Following the passage of the 1922 amendments, several continuing appropriation statutes and special funds were challenged under the terms of the amendment. In each of these cases interpreting Article 34, the Supreme Court held that the continuing appropriations statutes adopted prior to the 1922 amendments remained valid despite the new budget amendment. *See, e.g., Railroad Commission v. Riley,* 192 Cal. 54 (1923); *Board of Fish and Game Commissioners of the State of California v. Riley,* 194 Cal. 37 (1924); *see also Riley v. Thompson,* 193 Cal. 773 (1924); *Jamme v. Riley,* 192 Cal. 125 (1923); *Keiser v. State Board of Control,* 192 Cal. 129 (1923). In each of these cases, the California Supreme Court held that Art. IV, §34 did not repeal the appropriation statute at issue.

The most important of these early decisions is *Railroad Commission v. Riley,* 192 Cal. 54 (1923). The Railroad Commission sought a writ of mandate directing the state controller to settle the account of the Railroad Commission and to permit the deposit of fees the Commission had collected pursuant to a continuing appropriation provision of the Public Utilities Act. *Id.,* 192 Cal. at 55.

The State Controller opposed this application of funds, arguing that Article IV, §34 of the California Constitution constituted an implied repeal of all appropriations made prior to the enactment of

the amendment or, at a minimum, required that all appropriations be diverted into the general fund of the State. *Id.*, 192 Cal. at 56. The Controller argued that:

> [I]t was intended by the "budget amendment" to provide a scheme whereby each and every state expenditure, of whatsoever nature, during the biennial period following the enactment of the "budget bill," was to be provided in the "budget bill," and that the "budget bill" was to become the single and exclusive source of all state appropriations.... *Id.*, 192 Cal. at 56-57.

The California Supreme Court, however, rejected the argument that the budget bill was the sole source of appropriations:

> [T]he language employed in the California constitutional provision clearly indicates that the "budget bill" was not intended to become the single and exclusive source of all state appropriations. This necessarily follows from the fact that it is provided in the constitutional amendment itself that other appropriation bills may be enacted. *Id.*, 192 Cal. at 57.

The Supreme Court also rejected the Controller's argument that the budget bill converted all special funds into general funds:

> Clearly, it cannot be said that these provisions operate as an implied repeal of all appropriations by all statutes preceding the budget bill and that they thereby in effect do away with all special funds and convert such funds into part of the general fund...In the absence of some specific provision in the budget bill requiring that the special funds be transferred to the general fund, it would seem that the legislative intention is clearly shown to be that such special funds shall remain intact as special funds. *Id.*, 192 Cal. at 59.

Finally, the Supreme Court addressed the continuing validity of continuing appropriations in the face of silence in the budget bill on the matters covered by such appropriations:

> [T]he constitution here provides for inclusion in the budget of expenditures of the state, those provided by existing law, and so long as these expenditures remain expenditures provided by existing laws, they become part and parcel of the budget regardless of whether or not they are expressly set forth therein. *Id.*, 192 Cal. 54 at 58.

Within twelve months of its decision in *Railroad Commission v. Riley,* 192 Cal. 54 (1923), the California Supreme Court decided several similar cases. *See, e.g., Riley v. Thompson,* 193 Cal. 773 (1924); *Jamme v. Riley,* 192 Cal. 125 (1923); *Keiser v. State Board of Control,* 192 Cal. 129 (1923), *Osteopathic Examiners v. Riley,* 192 Cal. 158 (1923); *Western Shore Lumber Co. v. Riley,* 192 Cal. 144 (1923); *Riley v. Forbes,* 193 Cal. 740 (1924) and *Board of Fish and Game Commissioners of the State of California v. Riley,* 194 Cal. 37 (1924). In each of these cases, the California Supreme Court held the statutory appropriation at issue to be valid. Most of these opinions contain little analysis or discussion, merely a recitation of facts and a pronouncement that the case was controlled by *Railroad Commission v. Riley,* 192 Cal. 54 (1923).

In the last of the cases challenging the validity of pre-existing continuous appropriations, *Board of Fish and Game Commissioners of the State of California v. Riley,* 194 Cal. 37 (1924), the California Supreme Court stated that the aforementioned decisions established as "settled law" that the creation in 1909 and 1911 of a special fund in the state treasury benefitting the operations of the Fish and Game

Commission "created and constituted both a continuing fund and a continuing appropriation of the moneys deposited therein pursuant to said enactments and that said special fund so created and so to be disbursed was not abrogated or otherwise affected by the provisions of the budget amendment or budget bill....." *Id.*, 194 Cal. at 43. The California Supreme Court went on to recognize the right of the Governor to present a modified appropriation for approval by the legislature in stating that the continuing appropriation was not abrogated "except insofar as the Governor's said action carried into the budget law might be held to impose a limitation upon the amount of money available to the commission during the biennium provided for in said budget bill." *Id.*

As part of the present litigation, the Association has attempted to distinguish *Railroad Commission* and *Board of Fish and Game Commissioners* by arguing that in those cases, the continuing appropriations predated the new budget bill, so the issue "was the effect of a new budget amendment upon existing appropriations, which were in place; i.e. as in a previous budget year." Preliminary Opposition of Real Party in Interest Howard Jarvis Taxpayers Association and Steven White to Petitioner Kathleen Connell's Petition for Immediate Stay and Petition for Writ of Mandate, Prohibition or Other Appropriate Relief at 18.

These attempts to distinguish these cases under a "grandfather clause" analysis is inconsistent with the *Railroad Commission* case and the *Board of Fish and Game* case and demands the conclusion that, after the enactment of the budget bill amendment in 1922, no further concept of continuing appropriations (other than the "grandfathered" statutes) could exist (the Superior Court order in the *Jarvis* case so expressly states), a conclusion that is not supported, but refuted, by subsequent legislative, judicial and administrative precedent. In *Railroad Commission,* the Supreme Court used broad language stating that "the 'budget bill' was not intended to become the single and exclusive source of all state appropriations." *Railroad Commission v. Riley,* 192 Cal. at 57. The *Railroad Commission* court also pointed out that the provisions of the budget amendment in effect in 1922 (Article IV, §34 of the California Constitution) referred to inclusion in the budget presented to the legislature of all "proposed expenditures provided by existing law" and stated that such expenditures become a part of the approved budget, "regardless of whether or not they are expressly set forth therein." 192 Cal. at 58. This reference to "existing law" was deleted in 1966 when Article IV, §34 was amended slightly and moved to Article IV, §12, but no case directly addresses the effect of any such change on the validity of continuing appropriations statutes.

Several cases affirm the validity of continuing appropriations statutes enacted after the 1922 budget bill amendment, although none of these cases involved the issue of validity of the continuing appropriation under that amendment. *See, e.g., Riley v. Johnson,* 219 Cal. 513 (1933); *Daugherty v. Riley,* 1 Cal. 2d 298 (1934); *Gillum v. Johnson,* 7 Cal. 2d 744 (1936); *Urban v. Riley,* 21 Cal. 2d 232 (1942); *California Teachers Association v. Cory,* 155 Cal. App. 3d 494 (1984); *California Association for Safety Education v. Brown,* 30 Cal. App. 4th 1264 (1994). Statutes enacted in 1978 to overhaul the state budget and accounting process included reference to continuing appropriations: "On and after July 1, 1983, no moneys in any fund which by any statute other than a Budget Act, is continuously appropriated without regard to fiscal years, may be encumbered unless the Legislature, by statute, specifies that the moneys in the fund are appropriated for encumbrance." Section 13340 added by chapter 1284, Statutes of 1978 and discussed in 64 Op. Atty. Gen. Cal. 809. Section 13340 is apparently routinely amended in each budget act but repeats its recognition of continuing appropriations (the present version includes as an exception "the scheduled disbursement of any funds by a state or local agency or department that issues bonds and administers related programs for which funds are continuously appropriated as of June 30, 2000"). *See, also,* Government Code §16304 (stating that an "appropriation containing the term 'without regard to fiscal years' shall be available for encumbrance from year to year until expended" and exempting the following from any limitations imposed on the term of an appropriation–"[c]ontinuing provisions of law appropriating for specific purposes certain classes of revenue or other receipts, upon their deposit in a

particular fund in the State Treasury or upon their collection by an agency of this state"). Several opinions of the California Attorney General affirm that continuing appropriations are established under California law and are renewed each year without further legislative action. See 63 Op. Atty. Gen. Cal. 777 (1980) (a continuing appropriation statute "constitut[ed] a definitive self-executing continuing appropriation of the amounts therein so as to permit expenditures therefrom without further authorization - i.e., without provision thereof in the annual Budget Act.") and 64 Op. Atty. Gen. Cal. 809 (1981) (defining the elements of a proper continuing appropriation statute, including the use of the words found in Water Code §80200(a), "without regard to fiscal year").

The two most recent cases addressing continuing appropriation statutes are instructive. In *California Teachers Association v. Corey,* 155 Cal. App. 3d 494 (1984), petitioners sued for a writ of mandate to prevent the execution of a budget act's reduction of a prior statutory continuing appropriation to the Teachers' Retirement Fund on the grounds that allowing the reduction to be effective would impair a contract made by statute with beneficiaries of the fund, in violation of the "contract impairment" clauses of Article IV, §12 of the California Constitution and Article I, Section 10 of the U.S. Constitution. In finding such a contract impairment, the Court of Appeal necessarily assumed the prior validity of the continuing appropriation statute despite the subsequent action of the legislature in the budget process. In addition, the Court of Appeal sustained the petitioners' rejection of the claim that the "one item" provision of Article IV, §12(d) of the California Constitution was violated and, in so doing, the Court of Appeal did not raise any claim that Article IV, §12 overrides and supercedes any notion of a continuing appropriation. In *California Association for Safety Education v. Brown,* the Court of Appeal ruled that, in the absence of overriding action by the legislature in the budget process, a continuing appropriation "runs from year to year without the need for further authorization in the budget act." 30 Cal. App. 4th 1264 (1994).

Another case that lends some support for the general validity of continuing appropriations statutes is *People's Advocate, Inc. v. Superior Court*, 181 Cal. App. 3d 316 (1986). This case adjudicated the constitutionality of "the Legislative Reform Act of 1983," a statutory initiative that "made sweeping changes in the organization and operation of the Assembly and Senate and limits the content of future legislation which appropriates money for their operations." *Id.,* 181 Cal. App. 3d at 320. Section 9934 of the Legislative Reform Act limited the amount of money that could be appropriated by statute for the support of the Legislature to an amount determined by formula based upon previous budgets. *Id.,* 181 Cal. App. 3d at 239. The Court of Appeal held that Section 9934 was invalid, because it "invades not only the content of the Governor's budget bill but displaces the process (budget and budget bill) by which article IV, section 12, commands the adoption and enforcement of the budget." *Id.*

The portion of the case relevant to the validity of the continuous appropriation made by Water Code §80200(a) is in a footnote, where the Court of Appeal made clear that its ruling did not affect the general validity of appropriations by measures other than the budget, including by continuing appropriations:

> The limitation imposed by section 9934 upon the content of a budget measure must be distinguished from the constitutional authorization to appropriate money by statute by measures other than the budget bill. That power is specifically recognized in article IV, section 12. It authorizes the Legislature and hence the people to provide by statute for a continuing appropriation to pay for some specified program. (*See, e.g., Railroad Commission v. Riley* (1923) 192 Cal. 54, 218 P. 415.) However, the power so recognized does not authorize the placement of a legal limit upon the power of the Legislature to enact future appropriations legislation.

> Although as practical fiscal matter, a statute containing a continuous appropriation may limit the Legislature's *financial choices* in other appropriations measures, such a limitation is not one imposed by *law*. (*See* Leg. Rev. of the Budget, *supra*, p.182 *et seq*.) That is not the case here. The limitation mandated by section 9934 places legal limits upon the content of the legislation by which the Legislature is given the money to conduct its operations. That restriction exceeds the Legislature's own statutory power and hence exceeds the power of the people to do the same thing. *People's Advocate, Inc. v. Superior Court*, 181 Cal. App. 3d 316, 329 n.13 (1986).

Though this statement was not critical to the holding of the case, and thus is nonbinding dicta, it provides yet another indication of how California Courts of Appeal would tend to decide this issue.

Though it is not binding, a Historical and Statutory Note adopted by the Legislature provides further support for the validity of continuing appropriation measures generally. Section 151.4 of Stats. 1983, c.323, provides as follows:

> It is the intent of the Legislature that all items of appropriation be subject to annual review. The Legislature and the Governor recognize, however, that the public good may be best served by allowing certain items of appropriation to be continuously appropriated. Continuous appropriation status in no way removes the revenue or expenditures in these funds from annual adjustment in the Budget Act.
>
> The following criteria for which items should be continuously appropriated shall be used by the Legislature and the Executive Branch in the future in determining which items should be exempt from being continuously appropriated:
>
> (a) Bond funds and funds which derive revenues from the proceeds of bond sales may be continuously appropriated without regard to fiscal year for the purpose of payment of principal and interest.
>
> (b) Feeder funds through which revenues are allocated to secondary funds or local government for expenditure shall be continuously appropriated.
>
> (c) Proprietary and fiduciary funds from which tax refunds are made shall be continuously appropriated without regard to fiscal year.
>
> (d) Proprietary and fiduciary funds which do not contain General Fund monies and for which the state serves only as a trustee may be continuously appropriated.
>
> (e) Appropriations which would result in clearly demonstrable undue programmatic, administrative, or legal problems due to annual appropriation in the Budget Act may be considered for continuous appropriation.
>
> The Department of Finance shall annually, in the presentation of the Governor's Budget, provide the Legislature with a review of which funds are continuously appropriated, and suggest changes to the appropriation status to conform to this policy.

The leading case with regard to the "one item" requirement of Article IV, §12(d) is *California Teachers Association v. Cory,* 155 Cal. App. 3d 494 (1984), discussed above. As an alternative argument in that case, the Governor argued that the continuing appropriations statute in

question was invalid because it failed to comply with Article IV, §12 of the California Constitution. *Id.*, 155 Cal. App. 3d at 513. The Governor alleged that the continuing appropriations statute was unconstitutional because it violated the "one item" rule by appropriating money to multiple public entities. The Court of Appeal rejected that contention, citing the rule that "where a statute sets up a number of special funds for a single purpose, the allocations, considered together, should be treated as being only 'one item of appropriation.'" *Id.*, 155 Cal App. 3d at 513 (quoting *Metropolitan Water District v. Marquardt,* 59 Cal. 2d 159 (1963)). Thus, the Court of Appeal concluded that the continuing appropriation statute was "a valid appropriation." *Id.*, 155 Cal. App. 3d at 513.

The continuing appropriation contained in Water Code §80200(a) requires that all moneys in the Department of Water Resources Electric Power Fund (the "Fund") shall be appropriated to the Department and shall be available for the purposes of Division 27 of the Water Code (§80000 *et seq.*). The referenced division provides that the Fund and the moneys in the Fund are separate and distinct from any other fund and moneys administered by the Department. In addition, with respect to the Fund, Division 27 of the Water Code provides that the Department may issue revenue bonds not to exceed a certain amount. Because the statute serves one purpose -- providing for the use of the Fund and all moneys in the Fund for the purposes of Division 27 of the Water Code -- the measure does not violate the "one item" rule of Article IV, §12(d).

Conclusion

For these reasons, it is our view that, subject to the conditions and limitations set forth herein and based upon the consistent application of the principles enunciated in prior California decisions, the conclusion of the Superior Court judge in the *Jarvis* case questioning the validity of continuing appropriations, if and to the extent it would apply to payment of debt service on the Bonds and other amounts payable under the Agreement, is without merit and the California appellate courts would hold that the appropriations contained in the Appropriation Statute (and subject to the conditions set forth in the Appropriation Statute) are valid under the State Constitution and the State Controller may make payments pursuant to such appropriations.

Very truly yours,

Hawkins, Delafield & Wood

Hawkins, Delafield & Wood
633 West Fifth Street
Suite 3550
Los Angeles, California 90071

June 26, 2001

The Lenders under the Credit Agreement
mentioned hereinbelow

Morgan Guaranty Trust Company
of New York, as Agent
New York, New York

Fitch, Inc.
New York, New York

Moody's Investors Service, Inc.
New York, New York

Standard & Poor's Ratings Group
New York, New York

Ladies and Gentlemen:

We have acted as Bond Counsel to the California Department of Water Resources (the "Department") in connection with the execution by the Department of a Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement") among the State of California ("State") acting through the Department, various lenders ("Lenders"), and Morgan Guaranty Trust Company of New York, as Agent, pursuant to the Constitution and laws of the State, including Division 27 (commencing with Section 80000) of the California Water Code (the "Water Code"), added by Chapter 4 of the Statutes of 2001 (Assembly Bill No. 1 of the First Extraordinary Session of 2001) as approved by the State Governor on February 1, 2001 ("AB1X"), and as in effect on the date hereof (the "Act"), and Executive Order D-42-01 signed the State Governor on June 18, 2001 (the "Order").

Enacting AB1X, the Legislature found and declared the following:

> "The furnishing of reliable reasonably priced electric service is essential for the safety, health, and well-being of the people of California. A number of factors have resulted in a rapid, unforeseen shortage of electric power and energy available in the state and rapid and substantial increases in wholesale energy costs and retail energy rates, with statewide impact, to such a degree that it

constitutes an immediate peril to the health, safety, life and property of the inhabitants of the state, and the public interest, welfare, convenience and necessity require the state to participate in markets for the purchase and sale of power and energy." [Water Code §80000(a)]

Division 27 of the Water Code, enacted as part of AB1X, provides, among other things, as follows:

- Upon those terms, limitations, and conditions as it prescribes, the Department may contract with any person, local publicly owned electric utility, or other entity for the purchase of power on such terms and for such periods as the department determines and at such prices the Department deems appropriate. [Water Code §80100]

- The Department shall sell power directly to retail end use customers within the service area of the Electrical Corporations (as such term is defined in Section 218 of the California Public Utilities Code) that purchase power from the Electrical Corporations. [Water Code §80112]

- Upon the delivery of power to them, the retail end use customers shall be deemed to have purchased that power from the Department. Payment for any sale shall be a direct obligation of the retail end use customer to the Department. [Water Code §80104]

- The Department shall retain title to all power sold by it to the retail end use customers. [Water Code §80110]

- The Department may contract with the related Electrical Corporation for the Electrical Corporation to transmit (or provide for the transmission of) and distribute the power and provide billing, collection, and other related services, as agent of the Department, on terms and conditions that reasonably compensate the Electrical Corporation for its services. At the request of the Department, the California Public Utilities Commission (the "Commission" or "CPUC") shall order the related Electrical Corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute the power and provide billing, collection, and other related services, as agent of the Department, on terms and conditions that reasonably compensate the Electrical Corporation for its services. [Water Code §80106]

- All money collected with respect to any power acquired and sold, and all money paid directly or indirectly to or for the account of the Department with

respect to any sale, exchange, transfer, or disposition of power acquired pursuant to Division 27 of the Water Code, shall constitute property of the Department. To the extent any moneys are received by an Electrical Corporation pursuant to Section 80106 of the Water Code in the process of collection, and pending their transfer to the Department, they shall be segregated by the Electrical Corporation on terms and conditions established by the Department and shall be held in trust for the benefit of the Department. [Water Code §80112]

- The Department may fix and establish the procedure and charges for the sale or other disposal of power purchased by the Department. [Water Code §80120]

- The Department shall be entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to comply with Section 80134 of the Water Code, and shall advise the Commission as the Department determines to be appropriate. The Commission may enter into an agreement with the Department with respect to such charges. [Water Code §80110]

- The development and operation of a program as provided in Division 27 of the Water Code is in all respects for the welfare and the benefit of the people of the State, to protect the public peace, health, and safety, and constitutes an essential governmental purpose. [Water Code §80003(a)]

On January 17, 2001 the Governor of California issued a Proclamation pursuant to the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code, the "Emergency Services Act"), proclaiming to exist a state of emergency within California due to shortages of available electricity and ordering the Department to enter into contracts and arrangements for the purchase and sale of electric power with public and private entities and individuals as may be necessary to assist in mitigating the effects of the emergency (the "Emergency Proclamation").

On March 13, 2001 the Governor issued Executive Order D-30-01, thereby ordering the Department to implement a limited-term rate reward program for conservation efforts by residential, commercial and industrial customers of Electrical Corporations (the "20/20 Program"). On April 26, 2001 the Governor issued Executive Order D-33-01, thereby ordering the Department to implement a limited-term rate reward program for conservation efforts by residential, commercial and industrial customers of a particular Electrical Corporation: San Diego Gas & Electric Corporation (the "20/15 Program"). Under the 20/20 Program and the 20/15 Program, respectively, Electrical Corporations will provide rate reductions to consumers with credits of up to twenty percent of each customer's Summer 2001 bills for reducing

electricity consumption by at least twenty percent (or, for customers of San Diego Gas & Electric Corporation, by at least fifteen percent) during June to September 2001. The 20/20 Program and the 20/15 Program—as well as other governmentally sponsored or mandated energy conservation programs—will be funded through either or both of (i) payments by the Department to the Electrical Corporations ("Conservation Payments"), or (ii) reductions in payments to the Department that may otherwise be required of Electrical Corporations after September 2001.

On June 18, 2001 the Governor signed the Emergency Order to effectuate the purposes of the Emergency Services Act and to clarify and effectuate some features of the Emergency Proclamation.

In rendering the opinions expressed herein, we have assumed either that the Department will enter into a contract of the type referred to in Water Code §80106(a) with each Electrical Corporation in whose service area the Department sells power to retail end-use customers (each a "Service Agreement"), or that the Commission will issue an order of the type referred to in Water Code §80106(b) with respect to each such Electrical Corporation that does not enter into a Service Agreement (each a "Service Order"). We have also assumed that each Service Agreement and Service Order will, among other things, (i) require the Electrical Corporation to present regularly to each retail end-use customer an electric utility bill that includes a separate line-item clearly indicating the amount due for power sold to such customer by the Department, (ii) provide either for immediate transfer to the Department of moneys paid by retail end-use customers for power provided by the Department or for segregation of such collected moneys so that, pending their transfer to the Department, such collections will not be commingled with money of the Electrical Corporation but will be deposited into a denominated trust account at a bank within the State[1], (iii) acknowledge that such collections are made by the Electrical Corporation as agent of the Department and that moneys so collected are to be held by the Electrical Corporation as trustee for the benefit of the Department in accordance with Water Code §80112, and (iv) include terms and conditions, not inconsistent with the foregoing, that reasonably compensate the Electrical Corporation for its billing, collection and related services ("Servicing Fees"). We have assumed, further, that if the Electrical Corporation that is party to a Service Agreement is the debtor in a case commenced under the Bankruptcy Reform Act of 1978, as amended (the "Bankruptcy Code," codified as Title 11, United States Code), such

[1] Certain Electrical Corporations may remit such collections in an amount equal to estimated collections for the prior day. Such estimates will be further refined later. All of these estimates will be based on such Electrical Corporation's reasonable expectations, after reasonable inquiry, regarding the amounts that have been actually collected. The Electrical Corporation may be required to use estimates of collections rather than actual collections due to the limitations of such Electrical Corporation's payment processing and accounting systems. Each Electrical Corporation will provide to the Department a remittance report on a daily basis indicating the amount of money paid by retail end-use customers for power provided by the Department. We assume that these procedures establish segregation on terms and conditions acceptable to the Department within the meaning of Water Code §80112.

Service Agreement will be observed and performed at all times in accordance with a final order of the court approving its execution and performance by the Electrical Corporation, as debtor in possession, or by a bankruptcy trustee appointed in the case. We have also assumed the Commission will duly issue an order, independently of any rate-making for power sold by any Electric Corporation, in accordance with California law (including the Act and applicable rules and regulations of the Commission) and federal law, establishing a rate or rates for the sale to retail end-use customers of power purchased by the Department (as opposed to power sold by any Electrical Corporation), such that the rate or rates so established will not materially exceed the rate or rates sufficient to enable the Department to recover the revenue requirement described in Section 80134(a)(1)–(6) of the Water Code (a "Valid Rate Order").

As of this date the Department has not entered into a Service Agreement with any Electrical Corporation and the Commission has not issued any Service Orders. There has been no order, decision or other promulgation by the Commission that would constitute a Valid Rate Order for the purposes hereof, although the Commission has issued several decisions[2] concerning, among other topics: (i) electric utility rates applicable to power provided by each Electrical Corporation and the Department within the respective service areas of the Electrical Corporations, (ii) interim allocation of retail collections between the Department and each of the Electrical Corporations, and (iii) calculation of the California Procurement Adjustment defined in Section 360.5 of the California Public Utilities Code, enacted as part of AB1X (the "CPA," a portion of which—yet to be ascertained by the Commission—would determine the rate at which amounts are payable by each Electrical Corporation to the Department as the Fixed Department of Water Resources Set-Aside pursuant to Public Utilities Code §360.5). Furthermore, on April 6, 2001 Pacific Gas and Electric Company, one of California's largest Electrical Corporations ("PG&E"), commenced a voluntary case under Chapter 11 of the Bankruptcy Code; and on April 9, 2001 PG&E commenced an adversary proceeding against the Commission, seeking to invalidate certain orders contained in CPUC Decision 01-03-082 and to enjoin the enforcement of such orders[3]. On April 13, 2001 PG&E and Southern California Edison Company, another of California's largest Electrical Corporations ("SCE"), filed their separate applications for rehearing of CPUC Decision 01-04-005, concerning calculation of the CPA, alleging certain factual, Constitutional and other infirmities[4]. On April 27, 2001 SCE filed its application for rehearing of CPUC Decision 01-03-082, making the argument, *inter alia,* that

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[2] Including CPUC Decision 01-03-009, issued on March 9, 2001; CPUC Decision 01-03-082, issued on March 28, 2001; CPUC Decision 01-03-081, issued on March 29, 2001; and CPUC Decision 01-04-005, issued on April 4, 2001.

[3] By Memorandum Decision filed June 1, 2001, the United States Bankruptcy Court for the Northern District of California denied PG&E's application for injunctive relief and granted the Commission's motion to dismiss PG&E's complaint.

[4] On May 3, 2001 the Commission issued its Decision 01-05-037 denying the applications of PG&E and SCE for rehearing of CPUC Decision 01-04-005.

the Commission's allocation of electric revenues between SCE and the Department was unlawful and that portions of the decision effected an unconstitutional taking of SCE's property and a denial of due process of law.[5] In its application for rehearing of CPUC Decision 01-03-081, filed on April 30, 2001 (the "PG&E Application for Rehearing"), PG&E argues similarly that in requiring PG&E to remit funds to the Department for power purchases the CPUC committed an illegal taking of PG&E's property—in violation of the United States and California Constitutions—because it may require PG&E to pay to the Department revenues necessary to cover PG&E's authorized costs and thereby leave PG&E without a fair opportunity to recover those costs.[6] On June 4, 2001 PG&E and SCE filed with the California Court of Appeal their separate petitions for writ of review concerning CPUC Decision 01-04-005 and CPUC Decision 01-05-037.

You have requested our opinion as to whether—if an Electrical Corporation were to be or become the debtor in a case under the Bankruptcy Code—a federal court, exercising bankruptcy jurisdiction and reasonable judgment after full consideration of all relevant factors, would determine that moneys paid by retail end-use customers to such Electrical Corporation, acting as collection agent under the Service Agreement or pursuant to a Service Order (other than such customer payments in amounts equivalent to Conservation Payments, if any, and Servicing Fees), for power provided by the Department and at a rate or rates established in a Valid Rate Order, is property of the estate in such case, within the meaning of Section 541 of the Bankruptcy Code, that would be subject to the automatic stay under Section 362(a)(3) of the Bankruptcy Code.

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[5] In its application for rehearing of CPUC Decision 01-03-082, SCE has claimed that the property of a utility, although employed for the convenience of the public, belongs to the utility and cannot be taken from it without due process of law. See, Southern California Gas Co. v. PUC, 23 Cal. 3d 470, 476 (1979) ("The basic principle of ratemaking is to establish a rate which will permit the utility to recover its cost and expenses *plus* a reasonable return on the value of property devoted to public use."); Duquesne Light Co. v. Barasch, 488 U.S. 299, 308 (1989) ("If the rate does not afford sufficient compensation, the State has taken the use of the utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments."); Calfarm Insurance Co. v. Deukmejian, 48 Cal.3d 805 (1989). In view of such "Takings" and "Due Process" arguments and the possibility that the Commission—in the course of rate-design to implement Water Code §§80110 and 80120 relative to the Department's revenue requirement—may attempt to "allocate" to the Department all or a portion of pre-established rates or surcharges applicable to power sold by Electrical Corporations, it is not clear (and we express no opinion as to) whether a CPUC rate order establishing a rate or rates exclusively for the sale of power purchased by the Department that appears on its face to be issued independently of any rate-making for power sold by any Electric Corporation would, in substance, be a "Valid Rate Order."

[6] "[The Department] is authorized to set its actual revenue requirement under Water Code Sections 80110 and 80134(b), without reference to the CPA or to the utility's other rate components...". PG&E Application for Rehearing, p.4. "There is no financial or legal reason for the Commission to force PG&E to make the payments required by [CPUC Decision 01-03-081]. Under AB1X, [the Department] can fully recover its own costs of purchasing power directly from PG&E's customers, simply by specifying its precise revenue requirement under Water Code Section 80110." *Id.*, at 10.

Under Section 541(a) of the Bankruptcy Code, the commencement of a case under a chapter of the Bankruptcy Code for which a corporation is eligible creates an estate. Section 362(a)(3) of the Bankruptcy Code states that subject to certain limited exceptions, a petition in such a bankruptcy case operates as a stay, applicable to all entities, of "any act to obtain possession of property of the estate or of property from the estate[7] or to exercise control over property of the estate."

Section 323(a) of the Bankruptcy Code states that the trustee in a case under the Bankruptcy Code is the representative of the estate. Generally, the bankruptcy trustee may operate the debtor's business, as permitted in Section 1108. Also generally, a debtor in possession (*i.e.*, the debtor, if another person has not been appointed as bankruptcy trustee in the case) has all the rights and powers—and performs all the functions and duties—of a bankruptcy trustee. [11 U.S.C. §1107(a)]

The bankruptcy estate is comprised of, among other property, all legal or equitable interests of the debtor in property as of the commencement of the case and any interest in property that the estate acquires after the commencement of the case. [11 U.S.C. §541(a)(1),(7)] Section 541(d) of the Bankruptcy Code provides that property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest becomes property of the estate only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

There are facts and circumstances present with respect to the transmission and distribution of power purchased by the Department and the billing, collection and related services contemplated to be performed by each Electrical Corporation in connection therewith pursuant to the Act and a Service Agreement or Service Order that may raise issues regarding whether moneys paid by retail end-use customers for such power would constitute property of the related Electrical Corporation. We are not aware, however, of any decisions addressing power purchased and sold by the Department pursuant to the Act, or the retail payments in respect of such power, and thus the case law dealing with other rights to payment must be applied by way of analogy.

Although §541(a)(1) of the Bankruptcy Code is broadly worded, it does not define the terms "property" or "interest in property." Instead, §541(a) "merely defines what interests of the debtor are transferred to the estate. It does not address the threshold questions of the existence and scope of the debtor's interest in a given asset." In re Harrell, 73 F.3d 218

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[7] Property need not be "*of* the estate" in order to be "*from* the estate"—*i.e.*, in the possession of the estate—and therefore protected by the automatic stay. If, however, the property in question is not "property of the estate" and was not rightfully in the possession of the debtor at the time of commencement of the case, then Bankruptcy Code §362(a)(3) is inapplicable. See, *e.g.*, In re St. Clair, 251 B.R. 660 (D. N.J. 2000).

(9th Cir. 1995), citing In re Farmers Markets, Inc., 792 F.2d 1400 (9th Cir. 1986). The United States Supreme Court has confirmed that for bankruptcy law purposes questions regarding the definitions of "property" and "interests in property" are properly resolved by reference to state law. See, *e.g.*, Barnhill v. Johnson, 503 U.S. 393 (1992), citing Butner v. U.S., 440 U.S. 48 (1979) ("Congress has generally left the determination of property rights in the assets of the bankrupt's estate to state law"); In re Foam Systems Co., 92 B.R. 406 (B.A.P. 9th Cir. 1988).

In Teichman v. Teichman, 774 F.2d 1395 (9th Cir. 1985), the Ninth Circuit acknowledged that state law takes on importance in determining when a trust exists. ("The state may impose trust-like obligations on those entering into certain kinds of contracts, and these obligations may make a contracting party a trustee".) For instance, applying state law[8], the Ninth Circuit held that a statutory tax trust fund was created when debtors collected state and local sales taxes from their retail grocery store customers, and therefore traceable tax monies were not part of the bankruptcy estate, notwithstanding the lack of an identifiable trust fund. In re Megafoods Stores, Inc., 163 F.3d 1063 (9th Cir. 1998).

City of Farrell v. Sharon Steel Corp., 41 F.3d 92 (3rd Cir.1994), involved a controversy over municipal income taxes that the debtor withheld from its employees' wages before filing for bankruptcy protection. The Third Circuit found that under state (Pennsylvania) case law, when the debtor withheld the city income taxes a trust was created so that the debtor held the funds in trust for the city. Addressing the fact that the employer-debtor had possession of the funds it withholds prior to paying the employee, the court found that, in substance, when the employer pays the wages and withholds taxes it is paying the employees' taxes to itself since the employee has earned the entire gross wages.

> "Indeed, the only reason that the employer need not pay the funds withheld to the employee is that the applicable law requires the employer to withhold the wages for application on the employee's tax obligations. Thus, it would be artificial to characterize the withholding tax situation as simply creating a debtor-creditor relationship between the employer and the city. The real debt is the employees' tax liability to the city and the employer is merely the conduit for its employees' tax payments. Consequently, we hold that under [state] law [the debtor] held the withholding taxes in trust for the [city]."

Id. at 97. Consequently, the amount of the withholdings was determined not to be property of the estate.

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[8] Under Texas Tax Code §111.016, "[a]ny person who receives or collects a tax or any money represented to be a tax from another person holds the amount so collected in trust for the benefit of the state...."

Begier v. IRS, 496 U.S. 53 (1990), also concerned the treatment under Bankruptcy Code §541 of employees' taxes withheld by the bankrupt employer. The Supreme Court analyzed sections of the Internal Revenue Code (i) requiring an employer to collect Federal Insurance Contributions Act taxes from its employees by deducting the amount of the tax from the wages as and when paid, (ii) requiring an employer to deduct and withhold the employee's federal income tax, and (iii) stating, in 26 U.S.C. §7501, that the amount of taxes collected or withheld is "held to be in a special fund in trust for the United States." Before filing for bankruptcy protection, the debtor had paid to the IRS certain amounts due in respect of such withholdings, but not from accounts or moneys identified by the debtor as being held in trust. Since the genesis of the supposed trust was a federal statute, the Court did not need to examine any state laws to determine "interests of the debtor in property" for Bankruptcy Code §541 purposes.[9] The Court stated that the general common-law rule that a trust is not created absent a designation of particular property does not invalidate the creation by 26 U.S.C. §7501 of a trust in the "amount" of withheld taxes, since the common law of trusts is not binding on the legislature (in this case, Congress).[10] *Id.* at 63, fn. 4. Thus, payments of the withheld amounts to the IRS were not transfers of property of the debtor.

The legislative history of the Bankruptcy Code supports the proposition that when a debtor is a mere conduit for funds to travel from one party to another, it lacks an equitable interest in the money. As restated in In re Columbia Gas Systems Inc., 997 F.2d 1039 (3rd Cir. 1993), "the legislative history of [Bankruptcy Code §541][11] makes it clear that funds in the debtor's possession held for a third-party do not become part of the estate in bankruptcy." *Id.*, citing T & B Scottdale Contractors, Inc. v. U.S., 866 F.2d 1372, 1376 (11th Cir.), *cert. denied,* 493 U.S. 846 (1989). In Columbia Gas, the Third Circuit applied federal common

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[9] It should be noted, however, that "in general, preemption of state law is not favored 'in the absence of persuasive reasons—either that the nature of the regulated subject matter permits no other conclusion, or that Congress has unmistakeably so ordained.'" Matter of Quanta Resources Corp., 739 F.2d 912 (3rd Cir. 1984), *aff'd sub nom* Midlantic Nat'l Bank v. New Jersey Dep't of Environmental Protection, 474 U.S. 494 (1986), citing Consolidated Edison v. Montana, 453 U.S. 609, 634 (1981) (quoting Florida Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 142 (1963)). See also Stellwagen v. Clum, 245 U.S. 605 (1918) (state laws are suspended only to the extent of actual conflict with the scheme of federal regulation). Compare In re County of Orange, 191 B.R. 1005, 1015-17 (Bankr. C.D. Cal. 1996) (California law that property was held in trust by Orange County was preempted; County owned property).

[10] The validation of a trust without a res (in the case of trust-fund taxes for withholding) has its detractors. In his concurring opinion in Begier, Justice Scalia wrote: "A trust without a res can no more be created by legislative decree than can a pink rock-candy mountain." 496 U.S. at 70.

[11] "If the debtor holds bare legal title or holds property in trust for another, only those rights which the debtor would have otherwise had emanating from such interest pass to the estate under section 541." 124 Cong. Rec. 32,399 (1978) (House); *id.* at 33,999 (Senate).

law, rather than state law, in determining whether moneys subject to Federal Energy Regulatory Commission ("FERC") tariff orders were held in trust by the debtor. The application of federal law to the refund moneys at issue in Columbia Gas was based on the fact that such refunds were created by order of FERC and, therefore, the beneficiaries' interests therein were federally created property rights.[12]

In the context of construing non-bankruptcy statutes to determine the nature and extent of an estate's interest in property, the Ninth Circuit has stated that a statute should be read to give meaning to all of its parts. In re Pacific-Atlantic Trading Co., 64 F.3d 1292 (9th Cir. 1995). Division 27 of the Water Code was enacted as part of AB1X to address an electric power shortage "constituting an immediate peril" to California inhabitants and their property by having the State—through the Department—"participate in markets for the sale of power and energy." The Department is to purchase power and sell it to retail end-use customers, employing Electrical Corporations for power transmission and distribution and, as agent of the Department, for billing and collection of such sales price. It is reasonable to conclude that the Legislature intended such retail collections were to be used by the Department for, among other purposes, financing power purchases and paying debt service on Department indebtedness; for example, the Legislature required (in Section 80112 of the Water Code) that all such retail collections be transferred to the Department and deposited in a fund from which disbursements are restricted to program purposes such as additional power purchases, reimbursement for prior State appropriations for power purchases, payment of debt service on bonds issued to fund power purchases, and related costs and expenses, as described in Section 80200(b) of the Water Code. Mindful of the danger that the bankruptcy of one or more Electrical Corporations might pose to the Department's ability to purchase and sell power to retail end-use customers, the Legislature statutorily and unambiguously defined the Department's property interests in the pre-delivery power and post-sale retail collections; and, in so doing, the Legislature defined the Electrical Corporation's limited interest in such assets—

> "The department shall retain title to all power sold by it to the retail end use customers." [Water Code §80110]
>
> "All money collected with respect to any power acquired and sold pursuant to this division and the Governor's Emergency Proclamation dated January 17, 2001, and all money paid directly or indirectly to or for the account of the department with respect to any sale, exchange, transfer, or disposition of power acquired pursuant hereto, shall constitute property of the department and shall be deposited in the fund in accordance with subdivision (b) of Section 80200. To the extent any moneys are received by an electrical corporation pursuant to Section 80106 in the process of collection, and pending their transfer to the

[12] In comparison, the Department's interest in the retail sales proceeds of its power is a State-created right under Water Code §80112.

> department, they shall be segregated by the electrical corporation on terms and conditions established by the department and shall be held in trust for the benefit of the department." [Water Code §80112, emphasis added]

It is noteworthy that the debtor in possession, in the capacity of trustee in the bankruptcy case (and, as described above, the operator of the debtor's business), would be governed by 28 U.S.C. §959(b)[13], which states that—

> "Except as provided [for railroad reorganizations], a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof."

Based on and subject to the foregoing, as well as the limitations set forth below and the further qualification that there is no case directly on point, we are of the opinion that, should an Electrical Corporation be or become the debtor in a case under the Bankruptcy Code, and if the matter were properly briefed and presented to a federal court exercising bankruptcy jurisdiction, the court, exercising reasonable judgment after full consideration of all relevant factors, would determine that moneys paid by retail end-use customers to such Electrical Corporation, acting as collection agent under a Service Agreement or pursuant to a Service Order (other than such customer payments in amounts equivalent to Conservation Payments, if any, and Servicing Fees), for power provided by the Department and at a rate or rates established in a Valid Rate Order, is not property of the estate in such case, within the meaning of Section 541 of the Bankruptcy Code, and, therefore, that the Department's rights thereto would not be impaired by operation of Section 362(a) of the Bankruptcy Code.

We note that an Electrical Corporation's rights under a Service Agreement or pursuant to a Service Order (including rights to be paid Servicing Fees) may be property of the Electrical Corporation's bankruptcy estate; in addition, the Electrical Corporation may have possession of certain moneys paid by retail end-use customers for power provided by the Department. The Department and its transferee may be stayed from taking any acts that the court determines would have the effect of someone other than the Electrical Corporation obtaining possession of or exercising control over any such property.

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[13] In Quanta Resources, *supra*, the Third Circuit found that "[i]mplicit in Section 959(b) is the notion that the goals of the federal bankruptcy laws, including rehabilitation of the debtor, do not authorize transgression of state laws setting requirements for the operation of the business even if the continued operation of the business would be thwarted by applying state laws." 739 F.2d at 919.

In the event that an Electrical Corporation were to be or become a debtor under the Bankruptcy Code and it were asserted that the beneficial interest in and legal title to moneys paid by retail end-use customers for power provided by the Department were part of its bankruptcy estate, we express no opinion as to how long the Department or its transferee could be precluded from exercising remedies with respect to the Electrical Corporation or with respect to such retail collections before the validity of such an assertion could be finally decided. We also express no opinion as to whether in the event it were asserted that the beneficial interest in and legal title to any of the moneys paid by retail end-use customers for power provided by the Department were part of an Electrical Corporation's bankruptcy estate, a court would permit such entities to use such retail collections without the consent of the Department or its transferee, either before deciding the issue or pending appeal after a decision adverse to the Department or its transferee.

Legal opinions on bankruptcy law matters have inherent, unavoidable limitations that generally do not exist in respect of other legal issues on which opinions to third parties are typically given. These inherent limitations arise primarily because of (1) the pervasive equity powers of bankruptcy courts; (2) the potential relevance to the exercise of judicial discretion of facts and circumstances which may arise hereafter and (3) the nature of the bankruptcy process.[14] The recipients of this opinion should take these limitations into account in analyzing the bankruptcy risks associated with the subject transaction.

The outcome of litigation cannot be predicted with certainty. We note that a court's decision regarding matters upon which we opine herein will be based on such court's own analysis and interpretation of the factual evidence before it and of applicable legal principles. Thus, a different conclusion could be reached and would not necessarily constitute reversible error. Consequently, this opinion is not a prediction of what a particular court (including any appellate court) reaching the issue on the merits would hold, but instead is our opinion as to the proper result to be reached by a court applying existing legal rules to the facts as properly found (and consistent with the assumptions set forth herein) after appropriate briefing and argument. This opinion is not a guaranty, warranty or representation, but is merely this law firm's informed judgment as to a specific question of law.

We are members of the Bar of the State of California and we do not express any opinion herein as to any matter not governed by the laws of the State of California or by the Bankruptcy Code.

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[14] We note that the court may, on an interim basis, impose a temporary or preliminary stay with respect to moneys paid by retail end-use customers for power provided by the Department in order to afford itself time to ascertain the facts and apprise itself of the law. See, *e.g.*, In re Leisure Dynamics, 33 B.R. 171 (Bankr. D. Minn. 1983).

This opinion letter addresses the legal consequences of only the facts existing or assumed as of the date hereof. The opinions expressed herein are based on an analysis of existing laws and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted, events occurring, or changes in the relevant facts, after the date hereof. We have not undertaken to determine, or to inform any person of, the occurrence or nonoccurrence of any such actions, events or changes. We disclaim any obligation to update this opinion letter for events occurring or coming to our attention after the date hereof.

No attorney-client relationship has existed between our firm and any of the addressees in connection with the Agreement—or any of the transactions related thereto or contemplated thereby—or by virtue of this opinion letter.

Very truly yours,

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June 26, 2001

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Moody's Investor Service, Inc.
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Standard & Poor's Ratings Group
55 Water Street, 40th Floor
New York, New York 10041

The Agent and Lenders under the
Credit and Security Agreement
described below
c/o Morgan Guaranty Trust Company of New York,
as Agent

Ladies and Gentlemen:

We have acted as Special Counsel to the State of California Department of Water Resources (the "Department") in connection with the execution by the Department of a Credit and Security Agreement, dated as of June 26, 2001 (the "Credit Agreement") among the State of California ("State") acting through the Department, various lenders, and Morgan Guaranty Trust Company of New York, as Agent, pursuant to the Constitution and laws of the State, including Division 27 (commencing with Section 80000) (the "Act") of the California Water Code (the "Water Code"), added by Chapter 4 of the Statutes of 2001 (Assembly Bill No. 1 of the First Extraordinary Session of 2001) as approved by the Governor of the State on February 1, 2001 ("ABIX"), as in effect on the date hereof, and pursuant to Executive Order D-42-01 by the Governor of the State of California, dated June 18, 2001 (the "Executive Order").

Each of Pacific Gas & Electric Company ("PG&E"), Southern California Edison Company ("Edison"), and San Diego Gas & Electric Company ("SDG&E", and collectively with PG&E and Edison, the "Utilities") is a regulated electric utility with service areas within the State of California, that is engaged in, among other things, the transmission and distribution of electrical services to customers in its service territory. As used herein, "CPUC" means the California Public Utilities Commission; "CPUC Orders" mean such rules, regulations, decisions, opinions,

or orders issued by the CPUC from time to time in respect of the Act, including, without limitation Decision 01-03-081 dated March 27, 2001 (the "Interim Servicing Order"), establishing on an interim basis the allocation of retail collections between the Department and each Utility, Decision 01-03-82 dated the same date (the "Interim Rate Increase Order") providing for a rate increase of three cents per kilowatt-hour, Decision 01-05-064 dated May 15, 2001 (the "Interim Rate Allocation Order") imposing separate rates for each class of customers and Decision 01-04-005 dated April 3, 2001 (the "CPA Order") determining the California Procurement Adjustment for purposes of establishing the maximum amount of bonds that may be issued by the Department under the Act; "Customer" means a retail end use customer of a Utility; "DWR Power" means the electric power and energy, including, but not limited to, capacity and output, sold by the Department to Customers pursuant to the Act and CPUC Orders; "Utility Power" means electric power and energy, including, but not limited to, capacity and output, from a Utility's own generation, qualifying facility contracts, other power purchase agreements and bilateral contracts that are sold by a Utility to its Customers, but expressly excluding DWR Power; "DWR Charges" mean those charges assessed to Customers for DWR Power and any other amounts authorized to be collected pursuant to Sections 80110 and 80134 of the Water Code; "DWR Revenue" mean those DWR Charges collected by a Utility that are required to be remitted by such Utility to the Department; and "Utility Charges" mean those charges incurred by a Customer for Utility Power, as approved by the CPUC or other applicable governmental agency, but expressly excluding DWR Charges.

In January, 2001, the California Independent System Operator (the "ISO"), the operational manager of California's electricity transmission grid established by the Assembly Bill 1890, Chapter 854, California Statutes of 1996 (as amended, the "Deregulation Statute"), requested that the Department assist in avoiding rolling blackouts in the State by purchasing power in the spot market and delivering it to the ISO for redelivery to the Utilities as part of the supply to be made available to their customers. On January 17, 2001, the Governor of California issued a Proclamation pursuant to the California Emergency Services Act (Chapter 7, Division 1, Title 2 of the California Government Code, the "Emergency Services Act", the "Emergency Proclamation") proclaiming to exist a state of emergency within California due to shortages of available electricity and ordering the Department to "enter into contracts and arrangements for the purchase and sale of electric power with public and private entities and individuals as may be necessary to assist in mitigating the effects of this [energy shortage] emergency." Shortly thereafter, the Department began purchasing and selling power under a new, separate, statutory special fund known as the Department of Water Resources Electric Power Fund created pursuant to Senate Bill 7 (First Extraordinary Session of 2001), enacted on January 19, 2001. Under

ABIX, a more comprehensive program was created authorizing the Department to purchase electric power to be provided to Customers and to issue revenue bonds to finance those purchases. AB1X also authorized additional appropriations from the General Fund to the Electric Power Fund, pending issuance of the bonds. Since the enactment of the Act, the Department has spent several billion dollars to purchase power. On June 18, 2001 the Governor of California signed the Executive Order authorizing the Department to accept loans in an amount not to exceed in the aggregate (not including loans accepted to refund loans previously accepted hereunder) a principal amount of five billion dollars ($5,000,000,000) to mitigate the effects of the state of emergency. The Executive Order also granted to the Department, and directed it to exercise, the powers, authorities and rights described in Division 27 of the Water Code as it shall be amended upon the effective date of Statutes 2001, 1st Extraordinary Session, Chapter 9.

On April 6, 2001, PG&E filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code, 11 U.S.C. § 101 et seq. (the "Bankruptcy Code"). It currently maintains possession of its property and operates its business as a debtor in possession. To date, no other Utility has become the subject of a bankruptcy proceeding under the Bankruptcy Code.

You have requested our opinion as to whether in a case under the Bankruptcy Code in which a Utility is a debtor, a court would hold that the DWR Charges or the DWR Revenue collected by such Utility in respect of DWR Power constitute property of the estate of such Utility under Section 541(a)(1) of the Bankruptcy Code that would be subject to the automatic stay of Section 362(a)(3) of the Bankruptcy Code.

In connection with this opinion, we have reviewed the Act, the Interim Servicing Order, the Interim Rate Increase Order, the Interim Rate Allocation Order, the CPA Order, the Emergency Proclamation and the Executive Order (collectively, the "Documents"). This opinion is based solely upon our review of the Documents and our examination of such matters of law as we have deemed necessary for purposes of rendering the opinions set forth herein. As to factual matters, we have relied without investigation on the representations and warranties set forth in the Documents.

For purposes of this opinion, we have assumed, without investigation, that the following statements are or, as of the date of any bond issuance will be, correct:

1. Pursuant to Sections 80110 and 80134(b) of the Act, the Department has notified the CPUC of its revenue requirement in respect of DWR Power to be purchased by the Department in accordance with the Act.

2. Pursuant to the Act, the Department is authorized and directed to sell DWR Power directly to Customers of each Utility. The Department and the related Utility each tracks the amount of DWR Power being transmitted by or on behalf of the Department to such Utility's Customers on a daily basis.

3. AB1X provides that the Department owns all right, title and interest in and to the DWR Power and the DWR Charges derived in respect of the transmission and delivery thereof. No Utility asserts any interest in the DWR Power, other than as Servicer. No Utility takes any action that is inconsistent with the ownership of the DWR Power by the Department. Neither the DWR Power nor the DWR Charges are assets of any Utility under generally accepted accounting principles or any applicable tax or regulatory accounting principles purpose.

4. The CPUC, pursuant to Section 80110 of the Act, or the Department, pursuant to Section 80120 of the Act, will determine the amount of DWR Charges for DWR Power independently of any rates established, whether by the CPUC or otherwise, for Utility Power, and such DWR Charges will be measured solely as a function of the amount of DWR Power being sold to Customers by the Department, and not in any respect as a function of the amount of Utility Power being sold to the same Customers by a Utility.

5. Pursuant to the Act, the Department may, but is not required to, contract with the related Utility for the transmission and distribution of all power sold or to be made available for sale by the Department to Customers over such Utility's transmission and distribution system, and to provide billing, collection and related services, as agent for the Department, on terms and conditions that reasonably compensate such Utility for such services.

6. Either the Department will enter into a servicing agreement with each Utility (each, a "Servicing Agreement") or the CPUC will issue an order to each Utility as provided by AB1X (each, a "Servicing Order") to provide for the transmission and distribution of DWR Power to such Utility's Customers and to provide for the billing, collection and related services of the DWR Charges derived therefrom. The servicing compensation payable to the Utility will be compensation that constitutes a fair and reasonable price for the obligations to be performed by the Utility as Servicer under the related Servicing Agreement or the Servicing

Order. The Utility as Servicer is paid the full amount of the compensation payable to the Servicer. The obligation of a Utility as Servicer to indemnify the Department and certain transferees for breaches of its obligations under the related Servicing Agreement or the Servicing Order is of a type commonly found in transactions comparable to the transactions contemplated by the Documents and is unrelated to defaults on the DWR Charges.

7. Pursuant to the Act and the related Servicing Agreement or the Servicing Order, any bills sent by a Utility to its Customers will show amounts owed in respect of DWR Charges as a separate line item.

8. Pursuant to the Act and the related Servicing Agreement or the Servicing Order, the Utility as Servicer will remit collections on the DWR Charges to the Department or its transferee daily. Certain Utilities (including, for example, PG&E) may remit such collections in an amount equal to estimated collections on the DWR Charges for the prior day. Such estimates will be further refined not more than six months later. All of these estimates will be based on such Utility's reasonable expectations, after reasonable inquiry, regarding the amounts that have been actually collected. The Utility (including PG&E) may be required to use estimates of collections rather than actual collections due to the limitations of such Utility's payment processing and accounting systems. The time delay in refining the estimates is due to the limitations of such Utility's payment processing and accounting systems and the high costs and inefficiencies that would result from earlier or more frequent reconciliations. All amounts owed to the Utility as a result of such reconciliations are paid in full from collections on the DWR Charges. Moreover, each Utility will provide to the Department a remittance report on a daily basis indicating the amount of DWR Revenues collected by such Utility on behalf of the Department. We assume that these procedures establish segregation on terms and conditions that is acceptable to the Department within the meaning of Section 80112.

9. The Department reasonably believes that each Utility's procedures for determining the amounts of collections allocable to DWR Charges, taken together, will result in reasonable approximations of the actual collections with respect to DWR Charges in light of the limitations of the Utility's payment processing and accounting systems and the higher costs and inefficiencies that would result from attempting more accurate approximations. Neither the Department nor any Utility intends such procedures to mitigate losses that would otherwise be borne by the Department or its transferee.

10. No Utility is obligated to pay any insurance premiums in connection with any DWR Charges, any DWR Revenue or DWR Power, nor does any Utility pay any such premiums. No Utility reimburses any insurer for any losses such insurer suffers in connection with any DWR Charges, any DWR Revenue, or the Department's obligations under the Credit Agreement.

11. Each Utility is able to recover through the servicing fee or through its own rates and charges to its Customers the full amount of the Utility's operating costs (including return on invested capital) in respect of the services it provides under the Servicing Agreement or the Servicing Order in respect of the transmission and distribution to its Customers of DWR Power and the billing, collection and related services of the related DWR Charges, notwithstanding any provisions of the Act or the operation of market forces, so that the Utility does not suffer any losses as a result of payment defaults by Customers with respect to the DWR Charges, reductions in electricity consumption, or any other reason.

12. There are no other agreements to which the Utility is a party relating to the DWR Charges, other than the Documents and a Servicing Agreement or the Servicing Order.

13. No Utility makes any payments to the Department or its transferee, except pursuant to the Documents and the related Servicing Agreement or the Servicing Order.

14. No Utility receives any payments with respect to the DWR Charges, except pursuant to the Documents and the related Servicing Agreement or the Servicing Order.

15. Each of the Act, the Interim Order, any Servicing Order and any other CPUC Order which determines the amount of the DWR Charges, including, without limitation, any CPUC Order entered calculating the California Procurement Adjustment (as defined in Section 360.5 of the California Public Utilities Code, enacted as part of the Act) for purposes of the establishment of a Fixed Department of Water Resources Set-Aside, is valid and binding on the Utilities and the Customers without regard to the applicability of laws of general applicability relating to bankruptcy and the enforcement of creditors' rights. Each CPUC Order has been duly authorized and adopted by the CPUC. The Act and the CPUC Orders are each in full force and effect.

DISCUSSION

Section 541(a)(1) of the Bankruptcy Code provides that the commencement of a bankruptcy case "creates an estate . . . comprised of . . . all legal or equitable interests of the debtor in property as of the commencement of the case."

The United States Supreme Court has held that in bankruptcy "[p]roperty interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding." Butner v. United States, 440 U.S. 48, 55 (1979). Accord Barnhill v. Johnson, 503 U.S. 393, 398 (1992) ("In the absence of any controlling federal law, 'property' and 'interests in property' are creatures of state law"); Nobelman v. American Savings Bank, 508 U.S. 324, 329 (1993) (same). Relying on Butner, the United States Court of Appeals for the Ninth Circuit has explained:

> Although section 541(a) (1) [of the Bankruptcy Code] is broadly worded, it does not define the terms "property" or "interest in property." . . . Since the Bankruptcy Code itself does not determine the existence and scope of a debtor's interest in property, these threshold issues are properly resolved by reference to state law.

In re Harrell, 73 F.3d 218, 219 (9th Cir. 1996). Accord In re Jason Realty, L.P., 59 F.3d 423, 427-30 (3d Cir. 1995); In re Howard's Appliance Corp., 874 F.2d 88, 93 (2d Cir. 1989) (citing cases).

"Funds held in . . . trust present difficult property of the estate questions for courts." In re Cedar Rapids Meats, Inc., 121 B.R. 562, 567 (Bankr. N.D. Iowa 1990)); accord Gold Leaf Corp. v. Hamilton Projects, Inc., 78 B.R. 1018, 1021 (bankr. N.D. Fla. 1987) (noting "the difficulty in diagnosing . . . trust accounts in the context of § 541 property of the estate"). A court should resolve such questions based on the circumstances of the particular trust at issue. See In re World Communications, Inc., 72 B.R. 498, 500 (D. Utah 1987).

Section 80002.5 of the Act provides that:

> It is the intent of the Legislature that power acquired by the [D]epartment under this division shall be sold to all . . .

> [C]ustomers being served by a [Utility], and may be sold, to the extent practicable, as determined by the [D]epartment, to those local publicly owned electric utilities requesting such power.

Section 80104 of the Act further provides that:

> [u]pon the delivery of power to them, the ... [C]ustomers shall be deemed to have purchased that power from the [D]epartment. Payment for any sale shall be a direct obligation of the . . . [C]ustomer to the [D]epartment.

Section 80110 of the Act further provides in part:

> The [D]epartment shall retain title to all power sold by it to the ... [C]ustomers. . . .

Section 80112 of the Act expressly provides that, under California law,

> "[a]ll money collected with respect to any power acquired and sold [pursuant to the Act] ... and all money paid directly or indirectly to or for the account of the department with respect to any sale, exchange, transfer, or disposition of power acquired pursuant [t]hereto, shall constitute property of the department and shall be deposited in the [Electric Power] [F]und in accordance with [the terms of the Act]."

Furthermore, section 80112 provides that

> "[t]o the extent any moneys are received by an electrical corporation pursuant to Section 80106 in the process of collection, and pending their transfer to the department, they shall be segregated by the electrical corporation on terms and conditions established by the department and shall be held in trust for the benefit of the department."

Section 80116 of the Act provides in part:

> . . . Except to maintain system integrity, the [D]epartment shall sell the power that is to be delivered to . . . [C]ustomers with the service area of the [Utility] that purchase power from the [Utility] directly to the ... [C]ustomers.

The Interim Orders of the CPUC are to the same effect. The Interim Order provides in relevant part in its "order" paragraphs as follows:

> 3. SDG&E, Edison and PG&E shall segregate and hold in trust for DWR, no later than forty-five days after DWR supplies power to their retail end use customers an amount equal to the product of the number of kilowatt-hours that DWR 45 days earlier and the company-wide average generation-related rate [determined by paragraph 1]. . . .
>
> 5. Within 15 days of today's order, each utility shall file the tariff changes necessary to implement the more precise billing methodology set forth in this decision and shall implement billing under this more precise methodology within 30 days of the approval, by the CPUC or its staff, of the tariff changes.
>
> 6. In all cases funds and revenues that are to be paid to DWR shall be collected by the utility as agent for DWR, and segregated and held in trust for DWR in a separate bank account (denominated, "[utility name] in trust for the Department of Water Resources") for the benefit of DWR until such time as those funds shall be paid over the DWR in accordance with this order. . . . The utility shall not have any right in and to such funds and revenues, and such funds and revenues shall not be used by the utility as its own or commingled with its own monies. At all times such funds and revenues shall constitute property of DWR only, as provided by statute. Edison, PG&E, and SDG&E shall each transfer all funds held in trust accounts for DWR, including all

> interest paid thereon, each business day before 10:00 a.m., Pacific Time.

We have been advised by the Department that since the day following the effective date of D.01-03-81, each of the Utilities has been remitting revenues to the Department regularly.

The existence or amount of DWR Charges does not depend on the Utility supplying electricity to the Customers. Rather, the Customers are required to make payments in respect of DWR Charges if they consume DWR Power supplied by the Department. The Department is authorized to establish the rates at which its power is to be sold, or may contract with the CPUC for that purpose. The CPUC, pursuant to Section 80110 of the Act, or the Department, pursuant to Section 80120 of the Act, will determine the amount of DWR Charges for DWR Power independently of any rates established, whether by the CPUC or otherwise, for Utility Power, and such DWR Charges will be measured solely as a function of the amount of DWR Power being sold to Customers by the Department, and not in any respect as a function of the amount of Utility Power being sold to the same Customers by a Utility. Section 80120 of the Act provides:

> The [D]epartment may fix and establish the procedure and charges for the sale or other disposal of power purchased by the [D]epartment.

Section 80110 of the Act provides in part:

> The [D]epartment shall be entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to comply with Section 80134 [the statutory rate covenant for the benefit of bondholders and power providers], and shall advise the commission, as the department determines to be appropriate. . . . The commission may enter into an agreement with the department with respect to charges under Section 451 for purposes of this division . . . .

Power sold by the Department to Customers shall be allocated pro rata among all classes of customers, to the extent practicable. Thus, unless a Customer does not consume any electricity or consumes only self-generated electricity or electricity from an "alternate provider", the

Customer is liable in respect of DWR Charges, even if the Utility should no longer transmit or distribute the DWR Power sold by the Department to such Customers.

Thus, under the Act the Utilities have no rights in the DWR Power or the DWR Charges (and the collections thereon) derived therefrom. As a result, under the Butner line of cases, should a Utility become the debtor in a case under the Bankruptcy Code, the Utility would have no rights in the DWR Charges (and the collections thereon) and the DWR Charges (and the collections thereon) would not be property of the estate of the Utility under Section 541(a) of the Bankruptcy Code.

Some courts, however, have held that under certain circumstances, the Bankruptcy Code preempts state law concerning the rights of a debtor in property. E.g., Elliott v. Bumb, 356 F.2d 749, 754-55 (9th Cir. 1966) (state law that funds received by seller of money orders belonged to issuer of money orders was preempted; seller owned money); In re County of Orange, 191 B.R. 1005, 1015-17 (Bankr. C.D. Cal. 1996) (state law that property was held in trust by County was preempted; County owned property); In re Guardian Realty Group, L.L.C., 205 B.R. 1 (Bankr. D.D.C. 1997) (assignment of rents that was absolute under state law was only for security under the Bankruptcy Code). See also In re Unicom Computer Corp., 13 F.3d 321, 325 n. 6 (9th Cir. 1994) (state law establishing constructive trusts can be applied in bankruptcy only "in a manner not inconsistent with federal bankruptcy law"); In re KAR Dev. Assocs., L.P., 180 B.R. 597 (Bankr. D. Kan. 1994), aff'd, 180 B.R. 629 (D. Kan. 1995) (the court's power to carry out bankruptcy objectives does provide an adequate foundation for applying a federal rule rather than state law to define property interests where the situation demands. The [lower] court identified the objectives of equality of distribution and promotion of reorganization as sufficient justification for not applying state law . . . [.]).

Indeed, even a federal law that attempts to impose a trust by statute may be ineffective in bankruptcy if the subject of the trust cannot be identified. See, e.g., Begier v. Internal Revenue Service, 496 U.S. 53 (1991)(where funds withheld from employee paychecks for payment of federal income taxes and Federal Insurance Contributions Act (FICA) taxes and customer payments for excise taxes have been commingled with other assets of the debtor, the IRS must demonstrate that the "trust funds" are still in the possession of the debtor as of the commencement of the case); and see In re Columbia Gas Sys., 997 F.2d 1039, 1993 (3d Cir. 1993), cert. denied, 510 U.S. 1110 (1994) (the court held that federal common law, not state law, should govern for the following reasons: (1) the refunds at issue were created by an order of FERC and thus were derived directly from federal law; (2) applying state law to determine the

property rights in the refunds would frustrate the central purpose of NGA – to provide natural gas to the public at reasonable rates; and (3) some states' trust law requires some wrongdoing or unjust enrichment for the imposition of a constructive trust while federal common law imposes a trust whenever an entity acts as a conduit, collecting money from one source and forwarding it to its intended recipient).

Furthermore, some courts appear to have held that Section 541(a) (6) of the Bankruptcy Code (relating to proceeds) constitutes a countervailing federal interest that, under Butner, requires the preemption of state law. The result of these holdings is that property that would not be property of the debtor outside of bankruptcy is held to be property of the bankruptcy estate. Other courts have rejected such an argument. American Bankers Insurance Company v. Maness, 101 F.3d 358, 363-64 (4th Cir. 1996) (collecting cases on both sides of argument, but concluding that § 541(a) (6) does not preempt state law); In re Dias, 24 B.R. 542, 545 (Bankr. D. Idaho 1982) (court relied on § 541(a) (6) to invalidate an assignment that was absolute under state law). But see In re Louisiana World Exposition, 832 F.2d 1391, 1401 (5th Cir. 1987) (§ 541(a) (6) "does not give the bankrupt's estate property the debtor would not own if it were solvent").

There are facts and circumstances present with respect to the transmission and distribution of DWR Power and the billing, collection and related services of the DWR Charges pursuant to the Act and the Servicing Agreement or the Servicing Order which may raise issues regarding whether the DWR Charges would constitute property of the related Utility. We are not aware, however, of any decisions addressing the DWR Power or the DWR Charges, and thus the case law dealing with other rights to payment must be applied by way of analogy.

For example, pursuant to the Act, the Department may, but is not required to, contract with the related Utility for the transmission and distribution of all power sold or to be made available for sale by the Department to Customers over such Utility's transmission and distribution system, and to provide billing, collection and related services, as agent for the Department, on terms and conditions that reasonably compensate such Utility for such services. Section 80106 of the Act provides:

> (a) The department may contract with the related electrical corporation or its successor in the performance of related service, for the electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute the power, and provide billing, collection, and other

> related services, as agent of the department, on terms and conditions that reasonably compensate the electrical corporation for its services.
>
> (b) At the request of the department, the commission [the CPUC] shall order the related electrical corporation or its successor in the performance of related service, to transmit or provide for the transmission of, and distribute, the power and provide billing, collection, and other related services, as agent of the [D]epartment, on terms and conditions that reasonably compensate the electrical corporation for its services.

As set forth above, we have assumed that the Department will enter into a servicing agreement with each Utility or that there will be a valid Servicing Order to provide for the transmission and distribution of DWR Power to such Utility's Customers and to provide for the billing, collection and related services of the DWR Charges derived therefrom. The servicing compensation payable to each Utility will be compensation that constitutes a fair and reasonable price for the obligations to be performed by such Utility as Servicer under the related Servicing Agreement or the Servicing Order. Each Utility as Servicer will be paid the full amount of the compensation payable to the Servicer. The obligation of a Utility as Servicer under a Servicing Agreement or the Servicing Order to indemnify the Department or certain transferees for breaches of its obligations under the Servicing Agreement or the Servicing Order is of a type commonly found in transactions comparable to the transactions contemplated by the Documents and is unrelated to defaults on the DWR Charges. Pursuant to Sections 80110, 80120 and 801345 of the Act, the CPUC may be required to increase, at the request of the Department, or the Department independently could increase, the amount payable by the Customers on the DWR Charges to whatever amount is necessary to cause the bonds issued by the Department to be paid in full. Such increases could be necessitated by payment defaults by Customers or by decreases in electricity consumption. However, no Utility is bearing the risk of losses in respect of the DWR Charges. Instead, the Department and the CPUC have a duty imposed by the California Legislature to so increase the amount payable by the Customers.

In addition, Section 80106 of the Act provides that any Utility that provides transmission or billing and collection services to the Department in respect of the DWR Power or the DWR Charges shall be entitled to reasonable compensation for its services. As noted above, it is the reasonable expectation that each Utility will be able to recover through the servicing fee the full

amount of such Utility's servicing costs (including return on capital), notwithstanding any provisions of the Act or the operation of market forces, so that the Utility will not suffer any losses as a result of payment defaults by Customers with respect to the DWR Charges, reductions in electricity consumption, or any other reason. Thus, any increase in amounts payable in respect of DWR Charges is not expected to delay payment to the Utility of any Utility Charges past the date on which the Utility is otherwise legally entitled to receive such payments.

Each Utility acting as Servicer under a Servicing Agreement or the Servicing Order will remit collections on the DWR Charges to the Department or its transferee on a daily basis. Such remittances, however, may be made in an amount equal to estimated collections on the DWR Charges for the prior day. Such estimates will be refined not more than six months later. All of these estimates are based on the Utility's reasonable expectations, after reasonable inquiry, regarding the amounts that have been actually collected. It may be necessary to use estimates of collections rather than actual collections due to the limitations of a Utility's payment processing and accounting systems. The time delay in refining the estimates is due to the limitations of such Utility's payment processing and accounting systems and the high costs and inefficiencies that would result from earlier or more frequent reconciliations. If the reconciliation shows that such Utility owes the Department or its transferee money, then the Utility will be required to promptly make payment to the Department or its transferee. If the reconciliation shows that the Department or its transferee owes money to the Utility, then the Department or its transferee will promptly make payment to the Utility, and the Utility's right to reimbursement has priority over any payment to Agent. All such amounts owed to the Utility are paid in full from collections on the DWR Charges. Moreover, each Utility will provide to the Department a remittance report on a daily basis indicating the amount of DWR Revenues collected by such Utility on behalf of the Department.

The Department believes, after reasonable inquiry, that procedures of the Utilities for determining the amounts of collections allocable to DWR Charges, taken together, will result in reasonable approximations of the actual collections with respect to DWR Charges in light of the limitations of such Utility's payment processing and accounting systems and the higher costs and inefficiencies that would result from attempting more accurate approximations. Neither the Department nor any Utility intends such procedures to mitigate losses that would otherwise be borne by the Department or its transferee. As a result, the Utility's procedures for determining the amounts of collections allocable to DWR Charges do not constitute a form of recourse, but rather merely affect the timing of distributions to the Department or its transferee. Thus, if there are any losses, they will ultimately be borne by the Department or its transferee, not the Utility.

In addition, the Documents and the Servicing Agreement or the Servicing Order prohibit the Utility as Servicer from commingling collections with respect to the DWR Charges with its own funds. In In re Coupon Clearing Service, Inc., 113 F.3d 1091 (9th Cir. 1997), the court held that the fact that a servicer of coupons was permitted to commingle collections with its own funds required the conclusion that the collections were the property of the servicer. The court stated that "risk of loss . . . is a secondary factor, which is subordinate to commingling principles." 113 F.3d at 1101. Coupon Clearing Service appeared to consider only the ownership of the collections on the coupons, and did not consider the ownership of the coupons themselves. As noted below, we express no opinion herein as to collections in respect of the DWR Charges that are in the possession of the Utility and have been commingled with property of the Utility.

As indicated above, in accordance with the Act and the Servicing Agreement or the Servicing Order, bills sent by a Utility to its Customers on the DWR Charges will show amounts owed in respect of DWR Charges as a separate line item. Finally, the Department may replace or substitute the Utility as Servicer in accordance with the Servicing Agreement or the Servicing Order.

OPINION

Based on and subject to the foregoing, as well as the limitations set forth below and the further qualification that there is no case directly on point, we are of the opinion that, if a Utility were the debtor in a case under the Bankruptcy Code, and the matter were properly briefed and presented to a court, the court would hold that the DWR Charges (including the collections thereon) would not constitute property of the estate of the Utility under Section 541(a) of the Bankruptcy Code, and thus the Department's rights thereto would not be impaired by the operation of Section 362(a) of the Bankruptcy Code.

We note that we are not aware of any decisions interpreting the Act. Instead, judicial decisions in this area are usually made on the basis of an analysis of the facts and circumstances of the particular case. Furthermore, there are facts and circumstances present with respect to the transmission and distribution of DWR Power and the billing, collection and related services of the DWR Charges pursuant to the Act and the Servicing Agreement or the Servicing Order which we believe to be relevant to our conclusion but which, because of the particular facts at issue in the reported cases, are not generally discussed in the reported cases as being material factors. Moreover, the authorities we have examined contain certain cases and authorities that are arguably inconsistent with our conclusions expressed herein. These cases and authorities are,

however, in our opinion distinguishable in the context of the ownership of the DWR Charges pursuant to the Act.

We note that the Utility's rights to service the DWR Charges and its rights to be paid the servicing compensation will be property of the Utility's bankruptcy estate. The Department and its transferee may be stayed from taking any acts that the court determines would have the effect of someone other than the Utility obtaining possession of or exercising control over any such rights or over DWR Revenue in the possession of the Utility as of the commencement of the bankruptcy case.

We express no opinion as to any DWR Charges or collections thereon that are in the possession of the Utility and have been commingled with property of the Utility. Additionally, we note that the court may, on an interim basis, impose a temporary or preliminary stay with respect to the DWR Charges or the collections thereon in order to afford itself time to ascertain the facts and apprise itself of the law. See, e.g., In re Leisure Dynamics, 33 B.R. 171 (Bankr. D. Minn. 1983) (letter of credit) or may, on an interim basis, permit the relevant Utility to use collections from the DWR Charges without the consent of the Department or its transferee, either before deciding the issue or pending appeal after a decision adverse to the Department or its transferee.

We express no opinion herein as to (i) any matter not governed by the United States Bankruptcy Code, and thus we express no opinion regarding the laws of any state, (ii) the enforceability, perfection, validity, binding nature, or legality of the Act or any CPUC Order promulgated in respect thereof, (iii) any bankruptcy case affecting any entity other than a Utility, or (iv) any electricity charge other than DWR Charges, and the collections thereon.

All of the foregoing analyses and its conclusions are premised upon, and limited to, the law and the documents evidencing and governing the transactions described herein in effect as of the date of this letter. Furthermore, we note that a court's decision regarding matters upon which we opine herein is based on the court's own analysis and interpretation of the factual evidence before the court and of applicable legal principles.

Our opinions are subject to the effect of general principles of equity, including, without limitation, limitations on the availability of equitable remedies and concepts of materiality, reasonableness, good faith and fair dealing, and other similar doctrines affecting the enforceability of agreements generally (regardless of whether considered in a proceeding in equity or at law).

Our opinions are limited to the specific issues addressed and are limited in all respects to laws and facts existing on the date of this letter. The opinions set forth above are given as of the date hereof and we disavow any undertaking or obligation to advise you of any changes in law or any facts or circumstances that may hereafter occur or come to our attention that could affect such opinions. Furthermore, it is our and your understanding that the foregoing opinions are not intended to be a guaranty as to what a particular court would actually hold, but an opinion as to the decision a court should reach if the issue were properly presented to it and the court followed what we believe to be the applicable legal principles. In that regard, you should be aware that all of the foregoing opinions are subject to inherent limitations because of the pervasive equity powers of bankruptcy courts, the overriding goal of reorganization to which other legal rights and policies may be subordinated, the potential relevance to the exercise of judicial discretion of future-arising facts and circumstances and the nature of the bankruptcy process.

This opinion is solely for your benefit in connection with the transactions described in the first paragraph hereof and may not be relied upon or used by, circulated, quoted or referred to, nor may copies hereof be delivered to, any other person without our prior written approval. We disclaim any obligation to update this opinion letter for events occurring or coming to our attention after the date hereof.

Very truly yours,

Orrick, Herrington & Sutcliffe LLP

ORRICK, HERRINGTON & SUTCLIFFE LLP

Hawkins, Delafield & Wood
633 West Fifth Street
Suite 3550
Los Angeles, California 90071

June 26, 2001

The Bank of New York,
as custodian under the Custody Agreement
relating to RIBCO Trust Series 2001 FR/RI

Ladies and Gentlemen:

We have acted as Bond Counsel to the California Department of Water Resources (the "Department") in connection with the execution by the Department of a Credit and Security Agreement, dated as of June 26, 2001, among the State of California (the "State") acting through the Department, various Lenders and Morgan Guaranty Trust Company of New York, as Agent. You have requested our opinion as to whether the Department could become a debtor in a case under Chapter 9 ("Chapter 9") of the Bankruptcy Reform Act of 1978, as amended (the "Bankruptcy Code", codified as Title 11, United States Code (2000)).

Status of the Department under State Law

The Department is an administrative division of the Executive Branch of the California State government. See, *e.g.*, the following:

> "It is the policy of this State to vest in the Governor the civil administration of the laws of the State and for the purpose of aiding the Governor in the execution and administration of the laws to divide the executive and administrative work into departments as provided by law." Cal. Gov. Code § 11150 (West 2001).
>
> "Each department shall maintain an office and the director of each department who is member of the Governor's council shall reside at Sacramento. Each department shall adopt and keep an official seal." Cal. Gov. Code § 11151 (West 2001).
>
> "There are in the state government the following agencies: ... Resources ...." (emphasis added) Cal. Gov. Code § 12800 (West 2001).

"Each agency is under the supervision of an executive officer known as the secretary. Each secretary shall be appointed by, and hold office at the pleasure of, the Governor ...." Cal. Gov. Code § 12801 (West 2001).

"The secretary of each agency has the power of general supervision over, and is directly responsible to the Governor for, the operations of each department, office, and unit within the agency." Cal. Gov. Code § 12850 (West 2001).

"The secretary of each agency shall exercise the authority vested in the Governor in respect to the functions of each department, office, or other unit within the agency, including the adjudication of conflicts between or among the departments, offices or other units; and shall represent the Governor in coordinating the activities of each such department, office, or other unit with those of other agencies, federal, state, or local." (emphasis added) Cal. Gov. Code § 12850.4 (West 2001).

"The Resources Agency consists of ... the following departments: ... Water Resources." Cal. Gov. Code § 12805 (West 2001).

"There is in the Resources Agency the Department of Water Resources, which is under the control of an executive officer known as the Director of Water Resources. The director is appointed by the Governor and holds office at the pleasure of the Governor". Cal. Water Code § 120 (West 2001).

"Except to the extent inconsistent with the provisions of [the Water Code], the provisions of chapter 2 (commencing at Section 11150) [captioned: "State Department"], Part 1 [captioned: "State Departments and Agencies"], Division 3 [captioned: "Executive Department"], Title 2 [captioned "Government of the State of California"] of the Government Code shall govern and apply to the conduct of the Department of Water Resources in every respect the same as if such provisions were herein set forth at length, ..." Cal. Water Code § 124 (West 2001).

We have not, however, found any case law determining the status of the Department.

Required Nature of Debtor under Chapter 9 of the Bankruptcy Code

Section 109 of the Bankruptcy Code states in relevant part:

"(c) An entity may be a debtor under chapter 9 of this title if and only if such entity –

(1) is a municipality; [and]

(2) is specially authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter ...." (emphasis added)

The Department as an "Entity"

To be a debtor under Chapter 9, the Department must be an "entity" for purposes thereof. Under Section 101(15) of the Bankruptcy Code, an "entity" includes a person, estate, trust, governmental unit, and United States Trustee". Section 101(27) of the Bankruptcy Code defines "governmental unit" to include "a department, agency, or instrumentality of ... a State ...." Based on the foregoing, the Department is an "entity" for purposes of Section 109 of the Bankruptcy Code.

The Department as a "Municipality"

Section 101(40) of the Bankruptcy Code defines "municipality" to mean a "political subdivision or public agency or instrumentality of a State". None of these terms are defined in the Bankruptcy Code, and we have found no cases defining them. "Absent further definition, the boundaries of these terms are unclear, creating an inherent ambiguity as to what is and is not a municipality. The definition of a municipality in §101(40) is, therefore, ambiguous." *In re County of Orange*, 183 B.R. 594, 601 (Bankr. C.D. Cal. 1995).

The court in *In re County of Orange* examined the legislative history of Section 101(40), noting that the language in Section 101(40) is nearly identical to the language of Section 84 of 1976 municipal bankruptcy legislation: "Any State's political subdivision or public agency or instrumentality, which is generally authorized to file a petition under this chapter by the legislature ... is eligible for relief under this chapter ...." 11 U.S.C. §404 (1979). The court observed that Section 84 generally categorized a list of entities contained in Section 81 of the 1937 Bankruptcy Act (the "1937 Act"), as last amended in 1946, as follows:

> "... [C]ourts of bankruptcy shall exercise original jurisdiction as provided in this chapter for the composition of indebtedness of, or authorized by, any of the agencies of instrumentalities hereinafter named, payable (a) out of assessments or taxes, or both, levied against and constituting liens upon property in any of said agencies or instrumentalities, or (b) out of property acquired by foreclosure of any such assessments or taxes or both, or (c) out of income derived by such agencies or instrumentalities from any income-producing property, whether or not secured by a lien upon such property: (1) Drainage, drainage and levee, reclamation, water, irrigation, or other similar districts, commonly designated as agricultural improvement districts or local improvement districts, organized or created for the purpose of constructing, improving, maintaining, and operating certain improvements or projects devoted chiefly to the improvement of lands therein for agricultural purposes; or (2) local improvement districts, such as sewer, paving,

sanitary, or other similar districts, organized or created for the purposes designated by their respective names; or (3) local improvement districts, such as road, highway, or other similar districts, organized or created for the purpose of grading, paving, or otherwise improving public streets, roads, or highways; or (4) public-school districts or public-school authorities organized or created for the purpose of constructing, maintaining, and operating public schools or public-school facilities; or (5) local improvement districts, such as port, navigation, or other similar districts, organized or created for the purpose of constructing, improving, maintaining, and operating ports and port facilities; or (6) incorporated authorities, commissions, or similar public agencies organized for the purpose of constructing, maintaining, and operating revenue-producing enterprises; or (7) any county or parish or any city, town, village, borough, township, or other municipality ...."

The court concluded that "the term 'public agencies' was intended to replace the entities listed in (6) [of Section 81]. Further, it appears that the term 'political subdivisions' was intended to replace (7) [of Section 81] because each of the entities listed in (7) exercise sovereign powers of the state such as police power or the power to tax. See Texas Learning Tech. Group v. Commissioners of Internal Revenue, 958 F. 2d 122, 124 (5th Cir. 1992) ("The power to tax, the power of eminent domain, and the police power are the generally acknowledged sovereign powers.") This leaves "instrumentalities of a state" which, by default, must refer to the districts listed in (1)-(5)." *Id.* at 601, n. 16.

Political Subdivision

In re County of Orange involved three separate commingled investment funds (collectively, the "OCIP"). The Court found that the OCIP was not a political subdivision: "The OCIP does not possess the characteristics of a sovereign, unlike the entities in § 81(7), nor is it similar in any other respect to the political subdivisions described therein." *Id.* at 602. The Department, unlike the OCIP, may exercise the power of eminent domain. See, e.g., Cal. Water Code § 11575. However, as an administrative division of the State, the Department exercises such power on behalf of the State and not because such power has been delegated to it. See, e.g., People ex rel. Department of Water Resources v. Andresen et al., 193 Cal. App. 3d 1144, 1149 (Ct. of Appeal, 5th App. Dist., 1987) ("Acting through the Department of Water Resources, the State of California brought the condemnation action ....")

Public Agency

The court in *In re County of Orange* also found that the OCIP was not a public agency, which was defined in Section 81(6) of the 1937 Act as "incorporated authorities, commissions or similar public agencies organized for the purpose of constructing, maintaining and operating revenue producing enterprises ...." *In re County of Orange*, 183 B.R. at 602. The court found that the OCIP was not organized for these purposes.

The Department, pursuant to Division 27 (commencing with Section 80000) of the California Water Code, added by Chapter 4 of the Statutes of 2001 (Assembly Bill No. 1 of the First Extraordinary Session of 2001), the Emergency Proclamation dated January 17, 2001, of the State Governor, and Executive Order D-42-01 signed by the State Governor on June 18, 2001, and Division 6 of the California Water Code, operates revenue-producing power supply and water enterprises, and may issue bonds in connection with each such enterprise. The court in *In re County of Orange* did not consider the "incorporated" requirement of the definition, but the Department, as an administrative division of the Executive Department, is not an "incorporated" entity.

Control by Public Authority

An argument was made in *In re County of Orange* that "an entity is a municipality if it is subject to control by public authority, state or municipal". *Id.* at 602, n. 19. The court found, however, that in each of the cases cited for this proposition, it was assumed that the debtor was an agency and that the result turned on whether the agency was controlled by a governmental authority. As the court found that OCIP was not an agency, it determined that the cases and, thus, the argument were inapplicable to OCIP. Likewise, the Department, as an administrative division of the State government, is not controlled by the State; it is part of it.

Instrumentality of State

The court in *In re County of Orange* also concluded that the OCIP was not an instrumentality of the State, finding that "[t]he characteristics and objectives of the OCIP have nothing in common with the characteristics and objectives of these several entities described in §81 [(1)-(5) of the 1937 Act]." *Id.* at 603. The Department has some objectives in common with some of the entities described in Section 81 (1)-(5) of the 1937 Act, particularly in connection with its water supply activities under Part 3 of Division 6 of the Water Code, which can be analogized to water districts. However, all of the entities referred to in Section 81(1)-(5) are political subdivisions of the State or other organized or created entities, and not the State itself, while the Division is an administrative division of the State government. Accordingly, the Department does not share the characteristics of such entities.

Conclusion

Based on and subject to the foregoing, as well as the limitations set forth below and the further qualification that there is no case directly on point, we are of the opinion that if the matter were properly briefed and presented to a federal court exercising jurisdiction, the court, exercising reasonable judgment after full consideration of all relevant factors, would determine that the Department is not a municipality for purposes of Section 109(c)(1) of the Bankruptcy Code and, accordingly, cannot become a debtor under Chapter 9.

Department Not Authorized to File Under Chapter 9

Assuming, *arguendo*, that the Division is a municipality for purposes of Section 109 of the Bankruptcy Code, Section 109(c) would require express authority for it to file as a debtor under Chapter 9 of the Bankruptcy Code. The State has extended this authority to certain entities under Cal. Gov. Code Section 53760: "Any taxing agency or instrumentality of this State, as defined in Section 81 of the act of Congress entitled "An act to establish a uniform system of bankruptcy throughout the United States approved July 1, 1998, as amended, may file ...." The Department is not so defined.

Based on and subject to the foregoing, as well as the limitations set forth below and the further qualification that there is no case directly on point, we are of the opinion that if the matter were properly briefed and presented to a federal court exercising jurisdiction, the court, exercising reasonable judgment after full consideration of all relevant factors, would determine that the Department does not have express authority to file as a debtor under Chapter 9.

Legal opinions on bankruptcy law matters have inherent, unavoidable limitations that generally do not exist in respect of other legal issues on which opinions to third parties are typically given. These inherent limitations arise primarily because of (1) the pervasive equity powers of bankruptcy courts; (2) the potential relevance to the exercise of judicial discretion of facts and circumstances which may arise hereafter and (3) the nature of the bankruptcy process. The recipients of this opinion should take these limitations into account in analyzing the bankruptcy risks associated with the subject matter of this opinion letter.

The outcome of litigation cannot be predicted with certainty. We note that a court's decision regarding matters upon which we opine herein will be based on such court's own analysis and interpretation of the factual evidence before it and of applicable legal principles. Thus, a different conclusion could be reached and would not necessarily constitute reversible error. Consequently, this opinion is not a prediction of what a particular court (including any appellate court) reaching the issue on the merits would hold, but instead is our opinion as to the proper result to be reached by a court applying existing legal rules to the facts as properly found after appropriate briefing and argument. This opinion is not a guaranty, warranty or representation, but is merely this law firm's informed judgment as to a specific question of law.

We are members of the Bar of the State of California and we do not express any opinion herein as to any matter not governed by the laws of the State of California or by the Bankruptcy Code.

This opinion letter addresses the legal consequences of only the facts existing as of the date hereof. The opinions expressed herein are based on an analysis of existing laws and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by changes in the relevant facts after the date hereof. We have not undertaken to inform any person of, the occurrence of any such changes. We disclaim any obligation to update this opinion letter for events occurring or coming to our attention after the date hereof.

No attorney-client relationship has existed between our firm and any of the addressees in connection with the Agreement—or any of the transactions related thereto or contemplated thereby—or by virtue of this opinion letter.

Very truly yours,

Hawkins, Delafield & Wood

Hawkins, Delafield & Wood
633 West Fifth Street
Suite 3550
Los Angeles, California 90071

June 26, 2001

The Bank of New York, as custodian under the Custody Agreement relating to
RIBCO Trust Series 2001 FR/RI

Ladies and Gentlemen:

We have acted as bond counsel in connection with the execution and delivery by the State of California Department of Water Resources (the "Department") of a Credit and Security Agreement (the "Agreement") dated as of June 26, 2001, among the State of California (the "State"), acting through the Department, the lenders thereunder (the "Lenders") and Morgan Guaranty Trust Company of New York, as Agent. In that capacity, we have delivered to the California Department of Water Resources and the Lenders our approving opinion dated today's date relating to bonds issued pursuant to the Agreement (the "Bonds"). You are entitled to rely on said opinion as if the same were addressed to you.

We wish to notify you that we have also rendered opinions in connection with the execution and delivery of the Credit and Security Agreement relating to (i) certain bankruptcy matters and (ii) certain litigation concerning the validity of continuing appropriations. You may also rely on those opinions as well as if they were addressed to you.

Please note that this letter and the related opinion do not address the validity, the tax exemption, or any other matters relating to RIBCO Trust Series 2001 FR/RI or other interests in the Bonds issued by the Trust, as to all of which we express no opinion.

Very truly yours,

Hawkins Delafield & Wood

CERTIFICATE OF DEPARTMENT OF WATER RESOURCES
RELATING TO HISTORICAL ACTIVITIES

The California Department of Water Resources (the "Department") hereby certifies and represents as follows:

Under Part 3 of the California Water Code (the "Act"), the Department is responsible for the planning, construction and operation of the State Water Project, a complex of dams, water storage facilities, aqueducts, pumping stations and electric generation facilities which have been constructed by the Department for the purposes of developing a water supply and conveying water to areas of need within the State and providing flood control, recreation, fish and wildlife enhancement, hydroelectric power and other benefits. Pursuant to Section 11454 of the Act, the Department has the power to fix and establish the prices, rates, and charges at which the resources and facilities made available by the State Water Project shall be sold and disposed of, and to enter into contracts and agreements and do any and all things which in its judgment are necessary, convenient, or expedient for the accomplishment of its purposes and objects. The Act does not limit the ability of the Department to sell power to any person or entity.

The Department has been an active and significant participant in the power markets for many years. The historical scheduling of the Department's electric generating facilities of the State Water Project has resulted in the electricity generated by these facilities being insufficient for the needs of the State Water Project at certain times. As a result, the Department engages in extensive power acquisition activities. In addition, the Department has purchased power under long-term contracts with both public and private entities, and has entered the spot market for purchases from time to time. Over the last five years, the Department has solicited, negotiated and acquired by purchase or exchange in excess of 35,000 Gwh of electricity, both long-term and short-term, in connection with its State Water Project activities. The Department also from time to time has sold power from these facilities to utilities and others. By virtue of these activities, the Department has an interest in the stability of the power supply grid in California.

In addition, the Department has been a participant in the credit markets, having from time to time financed its activities by the issuance of over $5 billion of bonds and notes. As of May 1, 2001, $2,400,000,000 aggregate principal amount of revenue bonds of the Department were outstanding.

The Department also has an interest in the stability of the power supply grid in California by virtue of the water operations of the State Water Project, which in part involve electricity-powered pumping of water. Insufficient power supply, whether by curtailment or voltage reduction, could result in loss of pumping capacity and consequent loss of water supply.

The Department has determined, among other things, that the emergencies addressed by Chapter 4 of the Statutes of 2001 (Assembly Bill No. 1 of the 1st Extraordinary Session of

2001), as amended ("AB1X"), have affected its ability to perform its previously authorized duties and threaten the stability of the power supply grid on which it depends. The Department has determined that the activities authorized by AB1X and the Governor's Emergency Proclamation of January 17, 2001, which was issued pursuant to Sections 8550 et seq., of the Government Code, and Executive Order D-42-01, signed by the Governor on June 18, 2001, are necessary, convenient and expedient to enable it to continue to perform its preexisting duties and to stabilize the power supply grid upon which the State Water Project depends. Based in part on the foregoing, the Department also has determined that its duties under AB1X are similar and not foreign to those imposed under existing law, and are not more than additions to similar duties already imposed.

Dated: June 26, 2001.

CALIFORNIA DEPARTMENT OF WATER RESOURCES

by: Perla Netto-Brown

Perla Netto-Brown
Chief of Fiscal Services

CERTIFICATE OF CALIFORNIA DEPARTMENT OF WATER RESOURCES
AS TO INITIAL REVENUE REQUIRMENT AND ADVISEMENT THEREOF
TO THE CALIFORNIA PUBLIC UTILITIES COMMISSION

The California Department of Water Resources (the "Department") hereby certifies that attached hereto is a true and correct copy of the Department's initial revenue requirements. The Department advised the California Public Utilities Commission of these revenue requirements in accordance with 80134(b) of the Water Code on May 2, 2001.

Dated: June 26, 2001.

CALIFORNIA DEPARTMENT OF
WATER RESOURCES

By Perla Netto-Brown
Perla Netto-Brown
Chief of Fiscal Services

State of California The Resources Agency

Memorandum

Date : May 2, 2001

To: The Honorable Loretta Lynch, President
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

From : Thomas M. Hannigan
Department of Water Resources

Subject : Revenue Requirements

This letter is submitted by the Department of Water Resources in accordance with Division 27 of the California Water Code.

Section 80110 of the Water Code provides in part, "The Department shall be entitled to recover, as a revenue requirement, amounts and at the times necessary to enable it to comply with Section 80134, and shall advise the Commission as the Department determines to be appropriate." Section 80110 also provides that any "just and reasonable" review of its revenue requirements shall be conducted and determined by the Department.

Section 80134 of the Water Code provides that:

"(a) The Department shall, and in any obligation entered into pursuant to this division may covenant to, at least annually, and more frequently as required, establish and revise revenue requirements sufficient, together with any moneys on deposit in the fund, to provide all of the following:

(1) The amounts necessary to pay the principal of and premium, if any, and interest on all bonds as and when the same shall become due.

(2) The amounts necessary to pay for power purchased by it and to deliver it to purchasers, including the cost of electric power and transmission, scheduling, and other related expenses incurred by the department, or to make payments under any other contracts, agreements, or obligation entered into by it pursuant hereto, in the amounts and at the times the same shall become due.

(3) Reserves in such amount as may be determined by the Department from time to time to be necessary or desirable.

(4) The pooled money investment rate on funds advanced for electric power purchases prior to the receipt of payment for those purchases by the purchasing entity.

(5) Repayment to the General Fund of appropriations made to the fund pursuant hereto or hereafter for purposes of this division, appropriations made to the Department of Water Resources Electric Power Fund, and General Fund moneys expended by the department pursuant to the Governor's Emergency Proclamation dated January 17, 2001.

(6) The administrative costs of the Department incurred in administering this division.

(b) The Department shall notify the Commission of its revenue requirement pursuant to Section 80110."

In accordance with these and other provisions of the Water Code, the Department has determined and by this letter communicates to the Commission its revenue requirements, which are attached hereto as Exhibit A. The Department has determined that these revenue requirements are just and reasonable.

In developing the revenue requirements contained herein, the Department has made a variety of assumptions, including assumption relating to the following matters, among others: the amount of power to be purchased by the Department, the cost of such power, the amount of power which will be purchased pursuant to contracts, the amount of power which will be purchased on a "spot" basis, the impact of conservation efforts, the implementation of interim and long term financing, and interest rates applicable to such financing. Actual conditions may differ from those assumed by the Department, and any differences could have a material impact on the revenue requirements of the Department. Accordingly, the Department reserves its right to revise the revenue requirements as it determines necessary.

The Department requests that, in accordance with the provisions of Division 27 of the Water Code, the Commission establish specific rates payable to the Department for power sold by the Department to retail end use customers within the State. That is, the revenues resulting from such rates should be measured as a function of the amount of power sold by the Department and not in any respect as a function of the amount of power sold by the respective utility. Such rate or rates should be independent of rates payable by retail end use customers for power purchased by such customers from the utilities, and by law, must be sufficient in order for the Department to recover the revenue requirements attached hereto. It is critical that specific rates for Department power be established, so as to facilitate the identification and segregation of moneys collected from retail end use customers on behalf of the Department by the respective utilities, as required by Section 80112 of the Water Code.

If the Commission identifies a need for additional information to assist in the rate setting required by law, please notify the Department of such informational needs and the Department will endeavor to provide the necessary assistance. Please note however, that in order to allow the Department to continue to implement the power purchase program, it is necessary that certain information remain confidential.

Thank you for your assistance and attention to this important matter. We anticipate submitting additional information and requests to the Commission relating to the Department's power purchase program and financing plans and appreciate your continuing cooperation.

for Thomas M. Hannigan
Director
(916) 653-7007

Attachment

DWR Ratepayer Revenue Requirements
Combined
($000,000's)

Month	Power Purchase Commitments	Power Purchase Payments	Administrative Costs	Financing Costs	Total DWR Expenditures	Ratepayer Receipts From Past Power Sales	Other Revenues	Power & Bond Fund Interest Earnings	Expenditures of Bond Proceeds	Ratepayer Revenue Requirements	Total DWR Revenues	Power & Bond Fund Balance
Jan-2001	549.142	58.017	2.083	-	60.101	-	-	-	60.101	-	60.101	738.899
Feb-2001	1,447.839	687.754	2.083	-	689.838	32.746	-	3.079	654.013	-	689.838	1,580.642
Mar-2001	1,801.484	1,590.232	2.083	-	1,592.316	206.859	-	6.586	1,378.871	-	1,592.316	2,201.771
Apr-2001	1,780.914	1,983.127	2.083	-	1,985.210	334.137	0.356	9.174	1,641.543	-	1,985.210	2,068.522
May-2001	1,755.811	1,954.438	2.083	-	1,956.521	192.493	-	8.619	1,441.736	313.673	1,956.521	808.785
Jun-2001	1,123.225	1,473.687	2.083	-	1,475.770	-	17.303	3.370	808.028	647.069	1,475.770	0.757
Jul-2001	1,206.302	1,214.206	2.083	-	1,216.289	-	(90.184)	0.003	659.153	647.317	1,216.289	3,406.899
Aug-2001	1,286.883	1,242.338	2.083	-	1,244.421	-	(93.962)	17.140	630.401	690.843	1,244.421	2,776.498
Sep-2001	1,227.737	1,258.421	2.083	-	1,260.505	-	(93.676)	14.513	569.186	770.482	1,260.505	2,207.312
Oct-2001	1,215.860	1,303.035	2.083	-	1,305.119	-	(102.211)	12.141	618.189	777.000	1,305.119	1,589.124
Nov-2001	927.327	1,070.652	2.083	-	1,072.735	-	(92.743)	9.566	385.983	769.929	1,072.735	1,203.140
Dec-2001	991.719	961.639	2.083	-	963.722	-	(92.308)	7.957	329.149	718.924	963.722	873.991
Jan-2002	790.681	891.624	2.083	-	893.707	-	34.413	6.586	207.252	687.445	935.696	708.728
Feb-2002	615.577	698.654	2.083	-	700.738	-	33.574	6.046	21.370	699.236	760.225	746.846
Mar-2002	456.656	541.788	2.083	-	543.871	-	41.524	6.205	-	643.700	691.429	894.404
Apr-2002	537.541	490.282	2.083	-	492.365	-	39.101	6.820	4.788	592.739	643.447	1,040.697
May-2002	695.460	619.146	2.083	-	621.229	-	28.760	7.429	13.977	599.570	649.736	1,055.227
Jun-2002	714.747	626.156	2.083	-	628.239	-	43.679	7.490	10.289	655.760	717.218	1,133.917
	19,124.903	18,665.197	37.500	-	18,702.697	766.235	(326.374)	132.723	9,434.029	9,213.686	19,220.299	

DWR Ratepayer Revenue Requirements
Attributable to PG&E
($000,000's)

Month	Power Purchase Commitments	Power Purchase Payments	Administrative Costs	Financing Costs	Total DWR Expenditures	Ratepayer Receipts From Past Power Sales	Other Revenues	Power & Bond Fund Interest Earnings	Expenditures of Bond Proceeds	Ratepayer Revenue Requirements	Total DWR Revenues	Power & Bond Fund Balance
Jan-2001	337.731	35.682	1.313	-	36.994	-	-	-	36.994	-	36.994	466.408
Feb-2001	890.445	422.980	1.313	-	424.293	-	-	1.943	422.350	-	424.293	986.444
Mar-2001	1,107.943	978.019	1.313	-	979.332	74.979	-	4.110	900.243	-	979.332	1,346.280
Apr-2001	1,030.796	1,193.400	1.313	-	1,194.713	196.584	-	5.610	992.519	-	1,194.713	1,304.047
May-2001	1,032.933	1,154.039	1.313	-	1,155.352	119.893	-	5.434	862.729	167.296	1,155.352	555.985
Jun-2001	707.717	908.508	1.313	-	909.821	-	-	2.317	555.685	351.819	909.821	0.300
Jul-2001	635.096	705.001	1.313	-	706.313	-	(31.178)	0.001	387.888	349.602	706.313	1,818.137
Aug-2001	614.845	623.282	1.313	-	624.595	-	(31.178)	9.328	297.085	349.360	624.595	1,521.052
Sep-2001	672.326	644.713	1.313	-	646.026	-	(31.178)	8.090	302.629	366.485	646.026	1,218.423
Oct-2001	743.013	737.684	1.313	-	738.997	-	(31.178)	6.829	389.460	373.886	738.997	828.963
Nov-2001	620.527	680.974	1.313	-	682.287	-	(31.178)	5.206	315.207	393.052	682.287	513.756
Dec-2001	687.930	654.841	1.313	-	656.153	-	(31.178)	3.893	301.743	381.695	656.153	212.013
Jan-2002	505.795	595.524	1.313	-	596.836	-	22.633	2.636	190.465	381.102	596.836	21.548
Feb-2002	355.844	429.190	1.313	-	430.503	-	22.633	1.932	21.370	384.568	430.503	0.178
Mar-2002	214.851	286.890	1.313	-	288.203	-	24.357	1.843	-	336.849	363.050	75.025
Apr-2002	226.773	219.911	1.313	-	221.224	-	22.939	2.155	-	295.006	320.100	173.902
May-2002	323.202	276.512	1.313	-	277.825	-	22.633	2.567	-	282.235	307.435	203.512
Jun-2002	300.820	279.623	1.313	-	280.936	-	24.355	2.690	-	301.706	328.752	251.328
	11,008.587	10,826.775	23.627	-	10,850.402	391.455	(47.518)	66.584	5,976.367	4,714.663	11,101.552	

DWR Ratepayer Revenue Requirements
Attributable to SCE
($000,000's)

Month	Power Purchase Commitments	Power Purchase Payments	Administrative Costs	Financing Costs	Total DWR Expenditures	Ratepayer Receipts From Past Power Sales	Other Revenues	Power & Bond Fund Interest Earnings	Expenditures of Bond Proceeds	Ratepayer Revenue Requirements	Total DWR Revenues	Power & Bond Fund Ending Balance
Jan-2001	171.688	18.139	0.572	-	18.711	-	-	-	18.711	-	18.711	200.838
Feb-2001	452.663	215.025	0.572	-	215.597	-	-	0.837	214.760	-	215.597	397.081
Mar-2001	563.229	497.182	0.572	-	497.755	54.382	-	1.655	441.719	-	497.755	504.923
Apr-2001	576.577	626.496	0.572	-	627.069	121.670	0.259	2.104	503.036	-	627.069	416.335
May-2001	505.544	594.642	0.572	-	595.215	72.600	-	1.735	374.504	146.377	595.215	91.842
Jun-2001	285.700	398.579	0.572	-	399.151	-	11.897	0.383	91.621	295.250	399.151	0.221
Jul-2001	423.097	363.760	0.572	-	364.333	-	(58.988)	0.001	159.006	264.313	364.333	882.163
Aug-2001	504.847	461.184	0.572	-	461.756	-	(61.695)	4.463	251.419	267.570	461.756	630.744
Sep-2001	411.875	459.164	0.572	-	459.737	-	(61.567)	3.415	198.696	319.192	459.737	432.047
Oct-2001	341.291	415.226	0.572	-	415.799	-	(67.904)	2.587	163.722	317.394	415.799	268.325
Nov-2001	203.071	274.077	0.572	-	274.649	-	(61.661)	1.905	41.167	293.238	274.649	227.158
Dec-2001	194.613	200.516	0.572	-	201.089	-	(61.593)	1.734	4.541	256.407	201.089	222.617
Jan-2002	190.654	192.900	0.572	-	193.472	-	7.319	1.715	-	226.427	235.461	264.606
Feb-2002	176.850	181.463	0.572	-	182.035	-	6.838	1.940	-	232.477	241.255	323.825
Mar-2002	155.200	169.964	0.572	-	170.536	-	10.565	2.187	-	229.740	242.492	395.781
Apr-2002	220.143	181.560	0.572	-	182.132	-	10.725	2.486	-	222.150	235.361	449.009
May-2002	272.524	246.330	0.572	-	246.903	-	3.665	2.708	-	239.426	245.799	447.906
Jun-2002	283.526	247.720	0.572	-	248.292	-	12.608	2.704	-	274.144	289.456	489.069
	5,933.095	5,743.928	10.304	-	5,754.232	248.651	(309.531)	34.556	2,462.902	3,584.105	6,020.684	

DWR Ratepayer Revenue Requirements
Attributable to SDG&E
($000,000's)

Month	Power Purchase Commitments	Power Purchase Payments	Administrative Costs	Financing Costs	Total DWR Expenditures	Ratepayer Receipts From Past Power Sales	Other Revenues	Power & Bond Fund Interest Earnings	Expenditures of Bond Proceeds	Ratepayer Revenue Requirements	Total DWR Revenues	Power & Bond Fund Ending Balance
Jan-2001	39.723	4.197	0.198	-	4.395	-	-	-	4.395	-	4.395	71.654
Feb-2001	104.731	49.749	0.198	-	49.948	32.746	-	0.299	16.903	-	49.948	197.117
Mar-2001	130.312	115.031	0.198	-	115.229	77.499	-	0.821	36.909	-	115.229	350.568
Apr-2001	173.541	163.230	0.198	-	163.429	15.883	0.098	1.461	145.987	-	163.429	348.140
May-2001	217.334	205.756	0.198	-	205.955	-	-	1.451	204.504	-	205.955	160.958
Jun-2001	129.808	166.600	0.198	-	166.799	-	5.406	0.671	160.722	-	166.799	0.236
Jul-2001	148.109	145.445	0.198	-	145.643	-	(0.018)	0.001	112.259	33.402	145.643	706.599
Aug-2001	167.190	157.872	0.198	-	158.070	-	(1.089)	3.349	81.897	73.914	158.070	624.702
Sep-2001	143.536	154.543	0.198	-	154.742	-	(0.932)	3.008	67.860	84.805	154.742	556.842
Oct-2001	131.555	150.125	0.198	-	150.323	-	(3.129)	2.725	65.007	85.720	150.323	491.835
Nov-2001	103.729	115.601	0.198	-	115.799	-	0.096	2.454	29.609	83.639	115.799	462.226
Dec-2001	109.176	106.282	0.198	-	106.480	-	0.463	2.331	22.864	80.822	106.480	439.361
Jan-2002	94.233	103.201	0.198	-	103.399	-	4.461	2.235	16.787	79.915	103.399	422.574
Feb-2002	82.882	88.001	0.198	-	88.199	-	4.103	2.174	-	82.190	88.468	422.843
Mar-2002	86.605	84.934	0.198	-	85.132	-	6.602	2.175	-	77.111	85.888	423.598
Apr-2002	90.624	88.811	0.198	-	89.009	-	5.437	2.179	4.788	75.582	87.985	417.786
May-2002	99.733	96.303	0.198	-	96.502	-	2.462	2.154	13.977	77.909	96.502	403.809
Jun-2002	130.400	98.813	0.198	-	99.011	-	6.716	2.096	10.289	79.910	99.011	393.520
	2,183.221	2,094.494	3.569	-	2,098.064	126.128	30.675	31.583	994.759	914.919	2,098.064	

Addressee: Bill Lockyer,
Attorney General of the State of California

Re: Credit and Security Agreement
June 26, 2001

This letter is being provided with the understanding that it will be relied upon by you in issuing your opinion as to the validity of the Credit and Security Agreement, dated as of June 26, 2001, by and between the Department of Water Resources, the Lenders (as defined therein) and Morgan Guaranty Trust Company of New York, as Agent, (the "Credit Agreement"), and the bonds issued thereunder. It is my further understanding that I have been asked to provide information as to whether the loan accepted pursuant to the Credit Agreement (the "Interim Loan") is in mitigation of the electric power emergency proclaimed by the Governor of the State of California on January 17, 2001 (the "Emergency Proclamation").

I am the Deputy Director of the Department of Water Resources, and am the official within the Department responsible for implementation of the Department's power purchase responsibilities under the Emergency Proclamation and Division 27 (defined below). I hereby certify as follows:

As ordered by the Emergency Proclamation, and as authorized by Division 27 of the Water Code ("Division 27"), adopted in Statutes 2001, 1st Extraordinary Session, Chapter 4, and amended by Statutes 2001, 1st Extraordinary Session, Chapter 9, the Department of Water Resources, a department of the State of California, (the "Department"), has been purchasing electric power, both in the "spot market" and through long-term contracts. Division 27 established the Department of Water Resources Electric Power Fund (the "Fund"), and provided that the costs of the Department power purchases should be paid from the Fund. Division 27 also provided the Department with the authority to recover its "revenue requirements" from retail end use customers to which the Department supplied power, and provided for a continuous appropriation of moneys from the Fund to pay costs incurred by the Department pursuant to Division 27. While the Department has begun to recover a portion of its revenue requirements from charges collected from retail end use customers, approximately $8.3 billion has been appropriated from the State's General Fund to the Fund to help pay the costs of the Department's activities pursuant to the Division.

Pursuant to Division 27, the Legislature has authorized the Department to borrow funds for these power purchases and to replenish the General Fund through the issuance of long term bonds ("Division 27 Bonds"). Prior to the issuance of the Division 27 Bonds, it is necessary that certain arrangements be entered into by the Department, the electric corporations, and the California Public Utilities Commission. In addition, issuance of the Division 27 Bonds will require compliance with the requirements of the capital markets, including the receipt of long term credit ratings. Because of the large amount of Division 27 Bonds to be issued, the bonds cannot be issued all at one time, and must instead be issued over a period of several weeks. Because of these and other factors, the first date by which all of the Division 27 Bonds can be

issued, is presently expected to be no earlier than October of this year.

In compliance with the Emergency Proclamation and Division 27, the Department has entered into long-term power purchase contracts with various power providers. The rate paid by the Department for power purchased pursuant to these contracts is substantially less than the rate paid by the Department on the short-term, or "spot" market, and in that respect is a valuable contribution to the mitigation of the emergency established by the Emergency Proclamation.

Several of these long-term power purchase contracts permit the power supplier to terminate the contract if the Department does not issue bonds by June 30, 2001. These contracts represent approximately 68% of the power being purchased by the Department pursuant to long-term contracts in 2001.

In these contracts, "bonds" are sometimes defined as "bonds issued under" Division 27 and sometimes as bonds with specific credit rating criteria. The bonds issued pursuant to the Credit Agreement are not issued solely pursuant to Division 27, and the rating on the bonds issued pursuant to the Credit Agreement is not a published rating. No specific dollar amount of bonds is required by these contracts. While the short term Credit Agreement is not specifically contemplated by the contracts, bonds issued pursuant to the Credit Agreement, in an original principal amount of $4,300,000,000 can be reasonably expected to meet the power suppliers' credit criteria which is the underlying basis for the contract provisions requiring the issuance of bonds (as variously described), and I am advised by legal counsel to the Department (other than your office) that the ability of the Department to enforce these contracts (and prevent their termination) will be greatly enhanced by the execution of the Credit Agreement and the receipt by the Department of the funds thereunder.

Many of the contracts requiring the issuance of bonds by June 30, 2001, permit the Department to meet that requirement in the alternative by obtaining a credit rating on the Fund. Obtaining such a rating prior to June 30, 2001, is not practicable.

In addition to purchases pursuant to long term contracts described above, the Department also purchases significant amounts of power pursuant to "spot" and other short-term arrangements. The short-term power purchase market requires purchasers to either make same-day payment for purchases, or to provide evidence of credit-worthiness, as required by the various power suppliers. The State is unable to respond to same-day payment demands, and many large suppliers have imposed credit limits on the State, which range from approximately $150 million to as low as $15 million. When the Department's energy purchases reach a particular supplier's limits, the supplier suspends energy sales to the Department, and sales are not continued until payment is wired by the State.

This requires the Department to seek power elsewhere in the market, and can result in higher prices being paid by the Department and, in certain circumstances, the Department being unable to purchase sufficient power to avoid Stage 3 power alerts, and rolling blackouts. In particular, since January, 2001, these suspensions of energy sales resulted in rolling blackouts on several occasions and numerous Stage 3 power alerts.

While the Department took steps to meet spot market credit limits by putting letters of credit in place for certain power providers earlier this year, requirements of the long-term contracts that prohibit the Department from granting more favorable credit support to one power supplier over another, caused the Department to suspend the letter of credit program. No other alternative for establishing credit is available. (Because of limits to letter of credit capacity and other factors, it is infeasible to provide letters of credit for all power providers.)

The execution of the Credit Agreement will provide a tangible demonstration to power purchasers of the ability of the Department to make required payments pursuant to short term purchase arrangements, and will directly enhance the ability of the Department to purchase power in accordance with the Emergency Proclamation and Division 27.

In summary, for the reasons described herein, it is my view that execution of the Credit Agreement and the funding of the loan contemplated thereby in the amount of $4,300,000,000 will mitigate the impact of the emergency described in the Emergency Proclamation during the period prior to the issuance of the long term bonds.

I do not anticipate that the proceeds of any borrowing in the amount described above will be available, at any time prior to the issuance of the Division 27 Bonds, to reimburse the General Fund for disbursements made therefrom for the purchase of electric power.

Ray Hart
Deputy Director
Department of Water Resources

Addressee: Bill Lockyer,
Attorney General of the State of California

Re: Credit and Security Agreement
June 26, 2001

This letter is being provided with the understanding that it will be relied upon by you in issuing your opinion as to the validity of the Credit and Security Agreement, dated as of June 26, 2001, by and between the Department of Water Resources, the Lenders (as defined therein) and Morgan Guaranty Trust Company of New York, as Agent, (the "Credit Agreement"), and the bonds issued thereunder. It is my further understanding that I have been asked to provide information as to whether the loan accepted pursuant to the Credit Agreement (the "Interim Loan") is in mitigation of the electric power emergency proclaimed by the Governor of the State of California on January 17, 2001 (the "Emergency Proclamation").

I am the Director of Finance of the State of California and as such am familiar with the creation and financial aspects of the Department of Water Resources Electric Power Fund described herein and the financial condition of the General Fund. I hereby certify as follows:

As ordered by the Emergency Proclamation, and as authorized by Division 27 of the Water Code ("Division 27"), adopted in Statutes 2001, 1st Extraordinary Session, Chapter 4, and amended by Statutes 2001, 1st Extraordinary Session, Chapter 9, the Department of Water Resources, a department of the State of California, (the "Department"), has been purchasing electric power, both in the "spot market" and through long-term contracts. Division 27 established the Department of Water Resources Electric Power Fund (the "Fund"), and provided that the costs of the Department power purchases should be paid from the Fund. Division 27 also provided DWR with the authority to recover its "revenue requirements" from retail end use customers to which the Department supplied power, and provided for a continuous appropriation of moneys from the Fund to pay costs incurred by the Department pursuant to Division 27. While the Department has begun to recover a portion of its revenue requirements from charges collected from retail end use customers, approximately $8.3 billion has been appropriated from the State's General Fund to the Fund to help pay the costs of the Department's activities pursuant to the Division.

Pursuant to Division 27, the Legislature has authorized the Department to borrow funds for these power purchases and to replenish the General Fund through the issuance of long term bonds ("Division 27 Bonds"). Prior to the issuance of the Division 27 Bonds, it is necessary that certain arrangements be entered into by the Department, the electric corporations, and the California Public Utilities Commission. In addition, issuance of the Division 27 Bonds will require compliance with the requirements of the capital markets, including the receipt of long term credit ratings. Because of the large amount of Division 27 Bonds to be issued, the bonds cannot be issued all at one time, and must instead be issued over a period of several weeks. Because of these and other factors, the first date by which all of the Division 27 Bonds can be issued, is presently expected to be no earlier than October of this year.

Power purchases ordered by the Emergency Proclamation that are made between this date and October 31, 2001, are currently projected to be as high as $6 billion. Depending upon market conditions, the actual cost of power could be more or less than that amount. It is expected that revenues collected from retail end use customers will provide approximately $1,390,000,000 of such amount. Due to the potential negative impact of continuing General Fund advances on the State's perceived creditworthiness, at this time I believe it would be imprudent to advance further General Fund moneys (in excess of the $8.3 billion already appropriated) to the Fund.

For these reasons, I believe that the borrowing of $4,300,000,000 to fund purchases of power by the Department pursuant to Division 27 will mitigate the emergency established by the Emergency Proclamation.

I do not anticipate that the proceeds of any borrowing in the amount described above will be available, at any time prior to the issuance of the Division 27 Bonds, to reimburse the General Fund for disbursements made therefrom for the purchase of electric power.

Tim Gage
Director, California Department of Finance

REPORT OF PROPOSED DEBT ISSUANCE

California Debt and Investment Advisory Commission
915 Capitol Mall, Room 400, Sacramento, CA 95814
P.O. Box 942809, Sacramento, CA 94209-0001
Tel.: (916) 653-3269 FAX: (916) 654-7440

For Office Use Only
CDIAC #: _____

ompletion and timely submittal of this form to the California Debt and Investment Advisory Commission (CDIAC) at the above address will assure your compliance with existing California State law and will assist in the maintenance of a complete database of public debt in California. Thank you for your cooperation.[1]

ISSUER NAME: State of California Department of Water Resources

(If pool bond, list participants)

ISSUE NAME: Interim Energy Financing Bridge Loan

Please specify type/name of project:

PROPOSED SALE DATE: June 26, 2001 **PRINCIPAL TO BE SOLD:** $ 4,300,000,000 (Estimated)

IS ANY PORTION OF THE DEBT FOR REFUNDING?[2]

☒ No ☐ Yes, proposed amount for refunding $ _____

Issuer Contact:

Name: Perla Netto-Brown

Title: Director of Fiscal Services, Department of Water Resources

Address: 1416 9th Street, 11th Floor, Sacramento, California 95814

Phone: 916-653-9836 Issuer Located In Sacramento County

Filing Contact: Name of Individual (representing: ☒ Bond Counsel, ☐ Issuer, ☐ Financial Advisor, or ☐ Lead Underwriter) who completed this form and may be contacted for information:

Name: Kevin Civale

Firm/Agency: Hawkins, Delafield & Wood

Address: 633 West 5th Street, Los Angeles, CA 90071

Phone: 213-236-9050 E-mail: civalek@hdw.com

Send acknowledgement/copies to: Perla Netto-Brown, Chief, Division of Fiscal Services, Department of Water Resources, 1416 9th Street, 11th Floor, Sacramento, California 95814

FINANCING PARTICIPANTS:

BOND COUNSEL: Hawkins, Delafield & Wood, Los Angeles, California

FINANCIAL ADVISOR: Montague DeRose, Woodland Hills, California; Public Resources Advisory Group, Los Angeles, California

UNDERWRITER/PURCHASER: JPMorgan Chase & Co., Morgan Guaranty Trust Company of New York, Lehman Brothers, other lenders to be determined

IS THE INTEREST ON THE DEBT TAXABLE?

Under State law:	☒ NO (tax-exempt)	☐ YES (taxable)	
Under Federal law:	☒ NO (tax-exempt)	☒ YES (taxable)	$2,000,000,000 (Federal Tax Exempt) $2,300,000,000 (Federal Taxable)

If the issue is federally tax-exempt, is interest a specific preference item for the purpose of alternative minimum tax?

☐ Yes, preference item ☒ No, not a preference item

TYPE OF SALE: ☐ **Competitive** ☒ **Negotiated**

[1] *Section 8855(g) of the California Government Code requires the issuer of any proposed new public debt issue to give written notice of the proposed sale to the CDIAC no later than 30 days prior to the sale. Under California Government Code Section 8855(i), "The issuer of any new public debt issue shall, not later than 45 days after the signing of the bond purchase contract in a negotiated or private financing, or after the acceptance of a bid in a competitive offering, submit a report of final sale and official statement to the Commission. The Commission may require information to be submitted in the report of final sale that is considered appropriate."*

[2] *Section 53583(c)(2)(B) of the California Government Code requires that any local agency selling refunding bonds at private sale or on a negotiated basis shall send a written statement, within two weeks after the bonds are sold, to the CDIAC explaining the reasons why the local agency determined to sell the bonds at private sale or on a negotiated basis instead of at*

TYPE OF DEBT INSTRUMENT

NOTE

- ☐ Bond anticipation (BAN)
- ☐ Grant anticipation (GAN)
- ☐ Other note (Please specify below.) (OTHN)
- ☐ Revenue anticipation (RAN)
- ☐ Tax allocation (TALN)
- ☐ Tax and revenue anticipation (TRAN)
- ☐ Tax anticipation (TAN)
- ☐ Commercial paper (CP)
- ☐ Certificates of participation/leases (COPL)
- ☒ Other (Please specify below.) (OTH)

BOND

- ☐ Conduit revenue (Private obligor) (CRB)
- ☐ General obligation (GOB)
- ☐ Limited tax obligation (LTOB)
- ☐ Other bond (Please specify below.) (OTHB)
- ☐ Public lease revenue (PLRB)
- ☐ Revenue (Pool) (RB)
- ☐ Revenue (Public enterprise) (PERB)
- ☐ Sales tax revenue (STRB)
- ☐ Special assessment (SAB)
- ☐ Tax allocation (TAB)

Please specify if "Other note/Other bond/Other" was checked: Bond Anticipation Note, with term out provisions

SOURCE(S) OF REPAYMENT

- ☒ Bond proceeds (BDPR)
- ☐ General fund of issuing jurisdiction (GNFD)
- ☐ Grants (GRNT)
- ☐ Intergovernmental transfers other than grants (ITGV)
- ☐ Local obligations (LOB)
- ☐ Private obligor payments (POP)
- ☐ Other (Please specify.) (OTHS): _____
- ☐ Property tax revenues (PRTX)
- ☐ Public enterprise revenues (PER)
- ☐ Sales tax revenues (SATR)
- ☐ Special assessments (SA)
- ☐ Special tax revenues (SPTR)
- ☐ Tax-increment (TI)

PURPOSE(S) OF FINANCING

- ☒ Cash flow, interim financing (CFIF)
- ☐ Project, interim financing (PIF)
- ☐ College/university housing (CUH)
- ☐ Multifamily housing (MFH)[3]
- ☐ Single-family housing (SFH)[3]
- ☐ Health care facilities (HCF)
- ☐ Hospital (HOSP)
- ☐ Other/multiple health care purposes (equipment; etc.)(OMHC)
- ☐ College/university facility (CUF)
- ☐ K-12 school facility (KSCH)
- ☐ Other/multiple education uses (equipment, etc.)(OMED)
- ☐ Student loans (SLC)
- ☐ Redevelopment, multiple uses (RD)
- ☐ Commercial development (CMDV)
- ☐ Industrial development (INDV)
- ☐ Pollution control (PC)
- ☐ Airport (APRT)
- ☐ Bridges and highways (BRHI)
- ☐ Convention center (CCTR)
- ☐ Equipment (EQUP)
- ☐ Flood control/storm drainage (FLDS)
- ☐ Multiple capital improvements and public works (MCAP)
- ☐ Other capital improvements and public works (OCAP)
- ☐ Parking (PRKG)
- ☐ Parks/open space (PRKO)
- ☐ Ports and marinas (PRTS)
- ☐ Power generation/transmission (PWR)
- ☐ Prisons/jails/correctional facilities (PRSN)
- ☐ Public building (PB)
- ☐ Public transit (PTR)
- ☐ Recreation and sports facilities (RCSP)
- ☐ Seismic safety improvements/repair (SSI)
- ☐ Solid waste recovery facilities (SWST)
- ☐ Street construction and improvements (SCI)
- ☐ Wastewater collection and treatment (WSTW)
- ☐ Water supply/storage/distribution (WTR)
- ☐ Insurance/pension funds (IPF)
- ☐ Other than listed above (OTH)

Please specify type/name of project if different from above: _____

[3] *Certain local government issuers of housing bonds are required to obtain a certification from the State Treasurer attesting to their compliance with the State housing reporting requirements prior to issuance of the bonds to finance single- or multifamily housing.*