

EXHIBIT 2-B

AGREEMENT BETWEEN MONTEREY PENINSULA WATER MANAGEMENT DISTRICT AND CALIFORNIA AMERICAN WATER REGARDING REIMBURSEMENT FOR MITIGATION AND ASR ACTIVITY EXPENSES

THIS AGREEMENT is entered into this 24th day of September 2009, by and between California American Water (CAW) and the Monterey Peninsula Water Management District (MPWMD or Water Management District).

SECTION I FACTS

1. CAW and the Water Management District mutually desire to ensure cost-effective coordination of their activities, both joint and separate, relating to Aquifer Storage and Recovery (ASR) and Carmel River Mitigation programs.
2. The Water Management District was created by the California Legislature in 1977 (Statutes of 1977, Chapter 527, as amended). The California Public Utilities Commission (CPUC or Commission) acknowledged creation of the District in Decisions 89195 and 92793. Finding 16 of Decision 89195 provides, "The use of Monterey Peninsula water resources... and management of such resources can best be accomplished by the responsible local government agencies, coordinated when necessary with CAW and the Public Utilities Commission." Decision 89195 at Finding 18 also states, "As a result of Assembly Bill 1329 (Chapter 527) and a vote of the electorate in the area served by CAW's Monterey District, there is now in existence the Monterey Peninsula Water Management District, having very broad powers, including taxing powers."
3. The Water Management District, pursuant to ordinance, has imposed and collected a user fee from CAW customers continuously since 1983. The fee is based on actual water use and has been shown both on water bills for CAW and also on water bills for customers of the Seaside Municipal Water System. The user fee is expressed as a percentage of the meter and water charges, and most recently was set at 8.325 percent.
4. The MPWMD fee partially funds the comprehensive Mitigation Program and Aquifer Storage and Recovery (ASR) Program. The Mitigation Program lessens environmental impacts that result from community water use and CAW operations on the Carmel River and Seaside Groundwater Basins. These impacts have been determined to significantly affect the Carmel River populations of steelhead and red-legged frog, which are listed as threatened species under the federal Endangered Species Act. MPWMD uses general fund revenues to defray costs of the Mitigation Program and ASR programs that are not funded by its user fee.
5. State Water Resources Control Board (SWRCB) Order 95-10 (Order 95-10) recognized the MPWMD Mitigation Program. Ordering Paragraph 11 of Order 95-10 provides that CAW is to implement all measures in mitigation of the MPWMD Water Allocation Program if those are "not

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implemented by MPWMD.”

6. The ASR program enables excess winter flows from the Carmel River to be diverted and stored in the Seaside Groundwater Basin for use during the summer months in accord with guidelines set by federal and state fisheries agencies. CAW and MPWMD are joint owners of water rights under SWRCB Permit 20808A to allow Phase 1 of this ASR program. MPWMD and CAW jointly share work and responsibility for implementing Phase 1. ASR comprises an important aspect of the Monterey Peninsula’s water supply portfolio.

7. CPUC Decision 09-07-021, addressing issues related to the pass-through of the MPWMD water user fee to customers, states a concern that recovery of Water Management District costs from CAW customers by a surcharge on CAW customer bills must be shown to be appropriate. This Decision requires CAW to file an application addressing the manner in which ASR and Carmel River Mitigation program costs are funded. In the interim, CAW has filed an advice letter to record its interim costs.

8. CPUC Decision 09-07-021 is not the first time the topic of the Water Management District water user fee has been addressed by the Commission. The Commission recognized MPWMD’s authority to assess and collect fines from CAW customers in Decision 90-08-055. CPUC Decision No. 98-08-036 provided that rationing or moratorium measures for the Monterey Peninsula should be developed and administered by MPWMD. In particular, the Commission in 1994 reviewed a complaint filed by a CAW customer who objected to surcharges and administrative fees assessed by the MPWMD. Decision 94-03-015 examined the Water Management District’s 7.125% user fee, and MPWMD Ordinance No. 61, passed in July, 1992, that implemented the user fee. The Commission then noted that CAW “assesses on each bill a MPWMD fee of 7.125%, which it remits to MPWMD.” The Commission deferred interpretation of the ordinance to MPWMD.

9. CPUC Decision 09-07-021 does not authorize CAW to continue collection of the MPWMD surcharge at this time. In that decision, the CPUC noted that it lacked an adequate record to review the propriety of the user charges. The Commission also expressed concerns related to the reasonableness of the surcharge. Nonetheless, the CPUC directed CAW to file a subsequent application to demonstrate the reasonableness of the surcharge as a means to fund MPWMD mitigation and ASR activities.

10. MPWMD relies upon its user fee to fund its comprehensive Mitigation Program and ASR Program. But for these revenues, each activity would need to end. It is in the mutual interest of CAW, its customers, the Water Management District, and its constituents, to ensure uninterrupted protection of the Carmel River environment by continuation of MPWMD mitigation and ASR activities. CAW is otherwise and independently required by SWRCB Order 95-10 to implement all mitigation measures of the MPWMD Water Allocation Program to the extent those are not implemented by MPWMD.

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**SECTION II
PURPOSE**

This Agreement is needed to enable CAW to provide interim funding for the MPWMD Mitigation and ASR programs, and specifies terms and conditions upon which CAW shall fund MPWMD those activities. This Agreement is intended to address interim funding, pending a final decision by the CPUC on a subsequent application filed by CAW as contemplated in CPUC Decision 09-07-021.

Based upon the facts set forth in Section I, CAW shall pay to the Water Management District a monthly sum equal to a 8.325 percentage user fee on its meter and water charges, in accord with the practice that preceded Decision 09-07-021. This reimbursement agreement, however, shall be limited to the annual fiscal year payment of \$3,623,900.

**SECTION III
USE OF FUNDS**

The Water Management District shall use funds received pursuant to Section II exclusively to pay reasonable and necessary costs incurred to implement the MPWMD comprehensive Mitigation Program, and the MPWMD ASR Program. These costs shall include, but not be limited to, District labor and expenses, contract services, supplies and equipment.

**SECTION IV
OWNERSHIP OF WORK PRODUCT**

All original documents, explanations of methods, maps, tables, computer programs, reports, and other documents prepared under this Agreement and equipment purchased specifically for the project shall remain the exclusive property of MPWMD. CAW shall have an irrevocable, non-exclusive license to all original documents, explanations of methods, maps, tables, computer programs, reports, and other documents prepared under this Agreement, unless the granting of such license is otherwise prohibited. MPWMD shall in good faith attempt to negotiate the license provided by this section in the future procurement of goods or services acquired for the project.

**SECTION V
RESPONSIBILITIES**

In its performance of activities under this Agreement, the District shall act as an independent contractor and not as an agent or employee of CAW. CAW, for its part, agrees to provide access to information in its possession and cooperation of its staff in order to assist MPWMD and its contractor(s) to carry out its responsibilities herein. Any information CAW provides to MPWMD for the purposes of this agreement marked as "confidential" shall be treated in the same manner as "Confidential Information" is treated under the CAW-MPWMD Non-Disclosure Agreement dated June 22, 2009. The District shall have exclusive and complete control over its employees and subcontractors, and shall determine the method of performing the services hereunder.

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**SECTION VI
CHANGES AND CHANGED CONDITIONS**

If, during the course of the work herein contemplated, the need to change the purpose of this Agreement should arise, for whatever reasons, whichever party first identifies such need to change shall notify the other party in writing. The authorized representatives of the parties shall meet within seven (7) working days of the date of such notice, to discuss the need for change so identified and to determine if this Agreement should be amended. Any changes agreed to shall be documented by duly approved and executed amendments to this Agreement or other means acceptable to both parties.

**SECTION VII
TERMINATION**

Unless terminated earlier under the subsequent paragraph, this Agreement shall remain in effect until the date of final action by the CPUC on the subsequent application contemplated in Decision 09-07-021 relating to the MPWMD mitigation and ASR activities.

Any party may terminate this agreement at its convenience by providing the other party written notice in the manner specified in Section X at least 90 calendar days prior to the proposed termination date.

**SECTION VIII
SUBSEQUENT REVIEW BY CPUC**

The Water Management District and CAW each acknowledge CPUC Decision 09-07-021 does not provide present authority for CAW to collect the MPWMD user fee from CAW rate payers, that the CPUC will undertake a reasonableness review regarding the means by which the parties shall fund interim continuation of MPWMD mitigation and ASR activities, and that the Commission shall review a separate CAW application to regularly fund ongoing mitigation and ASR activities.

The Parties nonetheless deem this reimbursement agreement is essential to ensure uninterrupted protection of the Carmel River environment by continuation of MPWMD mitigation and ASR activities. MPWMD cannot continue those activities without this source of funds. CAW has filed an advice letter to record the interim costs associated with ASR and Carmel River Mitigation program costs.

As to any event where the CPUC disallows the request for reimbursement of recorded interim costs funded pursuant to this Agreement by reason of a finding that those activities undertaken by MPWMD were imprudent, or by a finding that the manner in which costs were incurred by MPWMD were not appropriate, MPWMD shall then reimburse those funds to CAW.

As to any other event where the CPUC disallows CAW's request for reimbursement of recorded interim costs funded pursuant to this Agreement, then and in those events CAW and MPWMD shall immediately meet and confer in an attempt to identify the reason(s) for disallowance, and shall agree

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as to how consequences of disallowance may be equitably shared between them. Should an agreed sharing of this risk not be reached within ninety (90) days after the date either party first requests resolution, the parties shall then select a mediator by requesting a list of seven (7) qualified arbitrators from the State Mediation and Conciliation Service. The parties shall flip a coin to determine who strikes first and shall alternate striking mediators until one name remains. The selected mediator shall provide a written recommendation as to how the parties shall equitably share the consequences of the disallowed interim costs, taking into account the amount of disallowance, the nature of the activity that was disallowed, and the long term benefits of that activity.

SECTION IX DISPUTES

In the event a dispute arises out of the performance of this Agreement, either party shall, as soon as a conflict is identified, submit a written statement of the conflict to the other party. Within five (5) working days of receipt of such a statement of conflict, the second party will respond and a meeting will be arranged not more than five (5) working days thereafter to arrive at a negotiated settlement or procedure for settlement. If, within twenty (20) working days from the initial filing of a statement of conflict an agreement cannot be reached, the parties agree to submit the matter to non-binding mediation. If meditation is unsuccessful, it is agreed that the dispute may be resolved in a court of law competent to hear this matter. This Agreement shall be construed in accord with California law. The prevailing party shall be awarded costs of suit and attorneys' fees.

SECTION X NOTICES

All communications to either party by the other shall be deemed given when made in writing and delivered or mailed to such party at its respective address, as follows:

MPWMD: Monterey Peninsula Water Management District
5 Harris Court, Bldg. G
Post Office Box 85
Monterey, California 93942

California American Water:

California American Water -- Monterey
511 Forest Lodge Road, Suite 100
Pacific Grove, California 93950

With a copy to:
Carrie Gleeson
Regional General Counsel
1033 B Avenue, Suite 200
Coronado, CA 92118

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**SECTION XI
RECORDS AND COOPERATION WITH CPUC**

MPWMD shall maintain complete and accurate records in accordance with generally accepted accounting practices for government agencies sufficient to show that funds received pursuant to Section II have been used exclusively to pay reasonable and necessary costs incurred to implement the MPWMD comprehensive Mitigation Program and the MPWMD ASR Program.

MPWMD shall fully assist and cooperate with CAW in responding to data requests issued by the CPUC regarding the purposes of this Agreement.

MPWMD and CAW shall fully assist and cooperate with each other in seeking authority for CAW to impose and collect a user fee from its CAW customers as a percentage of the meter and water charges in accord with past practice in order to fund the Mitigation and ASR Programs.

**SECTION XII
MUTUAL INDEMNIFICATION**

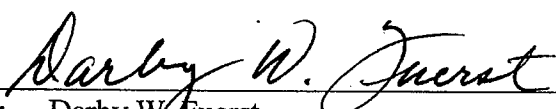
Each party shall indemnify, defend, protect, hold harmless, and release the other, its officers, agents, and employees, from and against any and all claims losses, proceedings, damages, causes of action, liability, costs, or expense (including attorney's fees and witness costs) arising from or in connection with, or caused by any negligent act or omission or willful misconduct of such indemnifying party. This indemnification obligation shall not be limited in any way by any limitation on the amount or type of damages or compensation payable to or for the indemnifying party under workers' compensation acts, disability benefit acts, or other employee benefit acts.

**SECTION XIII
AMENDMENTS**

This Agreement sets forth the entire understanding of the parties with respect to the subject matter herein. There are no other agreements expressed or implied, oral or written, except as set forth herein. This Agreement may not be amended except upon written amendment, executed by both parties hereto.

IN WITNESS WHEREOF, the parties hereto have entered into this Agreement effective as of the day and year first above written.

MONTEREY PENINSULA WATER MANAGEMENT DISTRICT


BY: Darby W. Fuerst
General Manager

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CALIFORNIA AMERICAN WATER



BY: Robert MacLean
President

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September 23, 2009