

• General Counsel's August 2005 Activity Report**Summary**

This report discusses significant matters in which the Legal Department was involved during the month of August 2005.

Attachments

None.

Detailed Report

1. Litigation/Claims To Which Metropolitan Is A Party**a. California Farm Bureau v. State of California**

In August, settlement was reached in this case involving a CEQA (California Environmental Quality Act) challenge brought by the California Farm Bureau on the EIR (Environmental Impact Report) for the Environmental Water Account Program (EWA). Earlier this year Metropolitan intervened in this case to protect our interests in the EWA Program. The final settlement lets the EIR stand and will not affect the current EWA Program.

b. Electric Industry Restructuring

On September 6, 2005, the Ninth Circuit issued its opinion concluding that the Federal Energy Regulatory Commission (FERC) exceeded its authority under the Federal Power Act (FPA) when it ordered governmental entities, including the California Department of Water Resources (CDWR/SWP), Metropolitan, and member agencies operating municipal electric utilities, to provide refunds for their sales of energy to the California Independent System Operator (ISO) and the California Power Exchange (PX) during California's energy crisis. The Court rejected every argument advanced by FERC in support of its refund order, finding that the FPA was "unambiguous" in its exemption of governmental entities from refund liability.

Unless the United States Supreme Court reverses the Ninth Circuit opinion, the State Water Project will *not* owe a net refund obligation to the ISO and the PX estimated to exceed \$30 million. Similarly, Metropolitan will not owe an estimated \$10,000 refund for sales of energy from Diamond Valley Lake. Metropolitan/SWC represented CDWR/SWP's interest at the refund hearing at FERC and in the preparation of appellate briefs because the California Attorney General represented California ratepayers who were adverse. A copy of the Ninth Circuit opinion, *Bonneville Power Authority v. Federal Energy Regulatory Commission*, No. 02-70262, can be found at [http://www.ca9.uscourts.gov/ca9/newopinions.nsf/340E07618AF6F116882570740058195B/\\$file/0270262.pdf?openelement](http://www.ca9.uscourts.gov/ca9/newopinions.nsf/340E07618AF6F116882570740058195B/$file/0270262.pdf?openelement).

c. Laub v. Davis; Regional Council of Rural Counties v. State of California

On August 30, 2005, Legal Department staff participated in oral argument before the Third District Court of Appeal in Sacramento on these consolidated cases that challenge the CALFED EIR. This appeal by the California Farm Bureau, Regional Council of Rural Counties, and the Central and South Delta Water Agencies seeks to overturn the lower court's decision upholding

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the EIR. Metropolitan is a respondent party to these consolidated cases and argued in support of the lower court's ruling to protect our interests in the CALFED process.

d. Shank/Balfour Beatty v. Metropolitan

On August 16, 2005, Metropolitan was served with a Notice of Appeal by pipe manufacturer Ameron. Metropolitan and Plaintiff Shank/Balfour Beatty settled their issues in June of 2004; however, the \$12 million dispute with Ameron continued into trial through December 2004. In March of this year the court ruled in Metropolitan's favor, finding that Metropolitan's termination of the original Arrowhead East and West construction contracts was proper and that Ameron is entitled to compensation of only the \$1.908 million that Metropolitan originally calculated and Ameron is not entitled to interest.

2. Other Matters Involving Metropolitan

a. State Water Resources Control Board Proposed Cease and Desist Order against DWR and Bureau of Reclamation

SWRCB issued on August 4, 2005 a notice of public hearing to determine whether it should adopt a cease and desist order against DWR (California Department of Water Resources) and the U.S. Bureau of Reclamation (USBR). SWRCB's Bay-Delta Water Quality Control Plan requires DWR and USBR to meet certain salinity objectives, including an electrical conductivity objective of 0.7 micro-mhos per centimeter at various points in the Southern Delta, effective April 1, 2005. If DWR and USBR had been able to install the permanent tidal gates that are part of the South Delta Improvement Program (SDIP), the objective would be relaxed to 1.0 mmhos/cm. Since the SDIP has not yet been implemented, DWR and USBR have notified SWRCB that the 0.7 mmhos/cm objective could be exceeded in some years. Although the objective has not been exceeded, SWRCB proposes to issue a cease and desist order requiring DWR and USBR to install and operate the tidal gates, or equivalent measures, by January 1, 2009 and to notify SWRCB of proposed corrective actions if a potential exceedance is projected, including releases of additional project water. A public hearing on the proposed order will be held on October 24, 2005. The State Water Contractors are working with DWR and USBR in preparation for the hearing and in implementing the SDIP program, including the tidal gates through the CEQA/NEPA (National Environmental Policy Act) and other regulatory processes.

b. U.S. EPA Issues Memo Addressing Necessity of NPDES Permits for Water Transfers under Clean Water Act

The U.S. Environmental Protection Agency (EPA), Office of General Counsel, recently published a memo responding to the question of whether the National Pollutant Discharge Elimination System (NPDES) permitting program set forth in the Clean Water Act applies to water control facilities that merely convey or connect navigable waters (water conveyances). The memo concludes that under most circumstances an NPDES permit would not be required for most water transfers. The issue of whether an NPDES permit is required for routine water transfers has been the subject of several important court decisions including the Supreme Court's holding in *South Florida Water Management Dist. v. Miccosukee Tribe of Indians* and the Court of Appeals decision in *Catskill Mountains Chapter of Trout Unlimited v. City of New York*.

In the memo EPA concludes that, based on the Clean Water Act as a whole, Congress intended to leave the oversight of water transfers to authorities other than state or federal NPDES program agencies. Individual state water resource management agencies would therefore be left with

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oversight responsibilities for most water transfer and related water quality issues. EPA also found that while resort to a case-specific evaluation of waters would not ordinarily be necessary or appropriate in light of Congressional intent, where such an evaluation was determined to be necessary, a permit would only be required for waters that were “meaningfully distinct.” The memo concludes with an indication that EPA will initiate a rulemaking process to more fully address water transfers.

3. Matters of Interest Not Involving Metropolitan

a. *Friends of the Everglades v. South Florida Water Management District*

The United States Department of Justice recently filed a summary judgment motion in *Friends of the Everglades v. South Florida Water Management District*. The matter, currently pending before the U.S. District Court for the Southern District of Florida, raises the question of whether an NPDES permit is required for three pump stations that convey water from four canals to the southern end of Lake Okeechobee. The government’s brief is significant in that it is entirely consistent with EPA's recent memo (see item above) finding that the Clean Water Act does not require NPDES permits for most water supply transfers.

Federal District Court Judge Cecilia Altonago has scheduled a hearing for early September on the factual issues of the case. A hearing on the legal arguments for summary judgment is expected later in the month. Metropolitan is participating in preparation of an amicus brief that will highlight the importance of unimpeded water transfers for western water users. The brief will support the government's position that the structure and language of the Clean Water Act and its legislative history support the conclusion that Congress did not intend to subject water transfers to the NPDES permitting program.

b. *Natural Resources Defense Council, et al. v. Rodgers, et al.*

Judge Lawrence Karlton of the Federal District Court in Sacramento has held that United States Fish and Wildlife (USFWS) and National Marine Fisheries Service (NMFS) Biological Opinions supporting renewal of water supply contracts for the Friant Division are inadequate. This is the most recent decision in a case filed in 1988 seeking to void renewals of the Friant water users’ 40-year contracts with the Bureau of Reclamation. The contracts had been renewed in 2000 after the Biological Opinions were issued finding that renewal would not jeopardize the delta smelt, central valley salmon, steelhead and other listed species. Judge Karlton held that the analyses were inadequate and ordered USFWS and NMFS to reinstate consultation with the Bureau and reconsider their Biological Opinions. The Judge did not order the renewed contracts to be rescinded.

c. *Natural Resources Defense Council, et al. v. Norton, et al.*

This action, challenging USFWS’ Biological Opinion regarding CVP (Central Valley Project) and SWP (State Water Project) proposed operations under the U.S. Bureau of Reclamation’s OCAP (Operations Criteria and Plan) has been moved from the Federal District Court in Oakland to Fresno. The State Water Contractors (SWC), who have appealed the Oakland judges’ refusal to allow SWC to intervene in support of the USFWS, are considering their options for further participation in this action.

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d. *Pacific Coast Federation of Fishermen's Associations et al. v. Gutierrez et al.*

A collection of environmental organizations has filed this action in the United States District Court in Oakland asserting that NMFS' Biological Opinion regarding the Bureau of Reclamation's Operations Criteria and Plan (OCAP) incorrectly found that the OCAP would not jeopardize salmon and steelhead. The June 2004 OCAP establishes the CVP's operational plan for diversion and distribution of water to its contractors and analyzes CVP's coordinated operations with the SWC. NMFS' Biological Opinion found that the OCAP, including SWP operations, would not jeopardize salmon or steelhead and provided incidental take authorization for the CVP and SWP. The State Water Contractors are preparing to intervene in support of NMFS. (A separate case—*Natural Resources Defense Council v. Norton*—by a similar group of plaintiffs alleges that USFWS' Biological Opinion inadequately considered OPAC's impact on the delta smelt.)

e. State Water Resources Control Board Review of the Bay-Delta Water Quality Control Plan

The State Water Quality Control Board held an additional day of testimony in its proceeding to review the 1995 Bay-Delta Water Quality Control Plan. The hearing focused on potential real-time flexible implementation of the Delta outflow ("X2") requirement. Flexible implementation would allow the fishery agencies to shift water from X2 use to upstream fishery needs or other beneficial uses when they determine the X2 benefit is not biologically significant. The State Water Contractors, including Metropolitan staff, testified in support of flexible operations.

4. Finances

The Legal Department assisted with documents for the potential sale of approximately \$100 million Water Revenue Refunding Bonds, 2005 Series C. When this opportunity to refund outstanding bonds was presented the financing team moved quickly to prepare the necessary documents and be ready to sell the bonds. The Legal Department updated Appendix A to the Official Statement, which contains relevant information about Metropolitan, and circulated the Appendix to the Board.