MEMORANDUM OF LAW

DATE: December 20, 1994

TO: Milon Mills, Director, Water Utilities

FROM: City Attorney

SUBJECT: City of San Diego's, Santa Fe Irrigation District's and San Dieguito Water District's Water Delivery and Storage Rights

By memorandum, you have asked our office to review an agreement among The City of San Diego ("the City"), the Santa Fe Water District and the San Dieguito Irrigation District (collectively referred to herein as the "Districts"). You have drafted a summary of what you believe to be the operational requirements of Lake Hodges pursuant to the agreement. (A copy of the operational assumptions is attached as Exhibit A.) A potential dispute has arisen between the City and the Districts regarding certain provisions of this agreement. You therefore have asked us to provide a legal opinion outlining the relative rights and obligations of the City and the Districts pursuant to the disputed provisions of the agreement, and to evaluate whether your operational assumptions are correct.

Background

Between 1925 and 1945, the City and the Districts entered into a series of contracts for the sale and delivery of water to the Districts. Disputes later arose among the parties regarding the quantity and quality of the water delivered by the City from Lake Hodges pursuant to the agreements. In order to settle the disputes, in 1956 the City and the Districts executed another agreement which resolved the rights and interests of the parties. Additionally, the agreement recognized that each of the parties had become a member of the San Diego County Water Authority since execution of their previous agreements and that they therefore were entitled to the delivery of varying amounts of water imported by CWA from sources outside of San Diego County.

As a result of changed circumstances, in 1969 the City and the Districts agreed to rescind all of the previous agreements and to enter into a new contract for the sale and delivery of water from the City to the Districts (the "1969 Agreement"). (A copy of the 1969 Agreement is attached as Exhibit B.) Included

in the 1969 Agreement was the sale from the City to the Districts of the San Dieguito Reservoir and Dam (including the conduit from the weir at Lake Hodges to the reservoir), the thirty-inch water transmission line originating at the CWA aqueduct, and all appurtenances necessary for the operation of these facilities. The 1969 Agreement expires on September 30, 2019.

At present, the City is in the process of negotiating with the CWA for the use of the Lake Hodges Reservoir for the storage of water. The proposed storage of water will be for emergency purposes for the region. The "re-operation" plans for emergency storage of water at the reservoir include connecting Lake Hodges to the Miramar Water Treatment Plant via the CWA aqueduct. The City has not utilized any of the water stored in Lake Hodges for itself in over thirty (30) years primarily because it does not have any connection from the reservoir to any of its water treatment plants.

The Districts have expressed concerns regarding the re-operation of the Lake Hodges Reservoir and believe it may threaten their perceived rights to water in the reservoir. In that context, Mr. Michael Cowett, counsel for the Santa Fe Irrigation District, reviewed the 1969 Agreement and provided an opinion regarding the Districts' water rights. (A copy of Mr. Cowett's opinion is attached as Exhibit C for your reference.) Summarizing, Mr. Cowett asserts the Districts' water rights pursuant to the 1969 Agreement are as follows:

1) The Districts have a property right to 7,500 acre feet of "local water" per year, if it is available. Local water is defined as water collected in Lake Hodges from any source other than water transported through the CWA aqueducts.
2) The City may not render local water unavailable to the Districts by selling or otherwise conveying the local water to any party prior to meeting its obligation of 7,500 acre feet of local water per year to the Districts.
3) The Districts' right to 7,500 acre feet per year of local water is a perpetual property right which endures beyond the term of the 1969 Agreement.

After analyzing the 1969 Agreement, we concur with Mr. Cowett's conclusion that the Districts have a perpetual property right to 7,500 acre feet of water per year from the City. However, where we depart from Mr. Cowett's opinion is in regard to what type of water the City must provide to meet its obligation to supply 7,500 acre feet of water per year. We believe the water provided by the City to meet its obligations pursuant to the 1969 Agreement may be either local water or imported water. Moreover, the City is entitled to beneficially use the local water from Lake Hodges for itself or sell it to others, under certain circumstances, without jeopardizing the water rights of the Districts. An analysis of the relevant provisions of the 1969 Agreement and applicable case law follows.

Analysis

I. GENERAL PRINCIPLES OF CONTRACT INTERPRETATION

The primary areas in dispute with respect to the 1969 Agreement are paragraphs 5, 7, and 8. These paragraphs read:

> 5. San Diego will sell to Districts all local water collected in Lake Hodges if said water is requested by Districts, provided that local water in Lake Hodges may be sold by San Diego to any other person, firm, corporation or agency if the following conditions exist:
>
> a. There is contained in Lake Hodges at the time water is delivered to such other entity a quantity of local water in excess of the quantity City is required to furnish Districts for the remainder of the water yearF
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> A "water year" commences on October 1 and ends On
>
> during which such sale is to be made; and
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> b. There will be in storage in Lake Hodges available for the exclusive use of Districts at the end of said water year not less than 8,300 acre feet of usable water; and
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> c. Said water is put to beneficial use by the purchaser.

> San Diego may also release water from Lake Hodges in emergency to prevent or reduce flood or threat of flood damage.
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> 7. San Diego will deliver a total quantity of at least 20,000 acre feet of local water to Districts during each "ten-year period" during the term of this agreement. The first such "ten-year period" actually contains 10= years, and will terminate with the end of the water year expiring on September 30, 1979. Each subsequent 10-year period will contain 10 years. If the quality of local water becomes unacceptable to the San Diego County Health Officer for domestic consumption after coagulation and filtration or if no local water is available in Lake Hodges for delivery to Districts, San Diego will supply water from alternate sources which shall be of a quality acceptable to the San Diego County Health Officer after coagulation and filtration.
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> 8. In addition to Districts' entitlement to water transported through the San Diego County Water Authority's aqueducts, San Diego upon request of Districts will furnish Districts a total quantity during each water year of 7,500 acre feet of local or imported water of a quality acceptable to the San Diego County Health Officer for domestic consumption after coagulation and filtration.

(Emphasis added.)

Generally, contracts must be interpreted so as to give effect to the mutual intention of the parties as it existed at the time of contracting, to the extent the same is ascertainable and lawful. Cal. Civ. Code section 1636. The entire agreement must be construed as a whole and each clause considered in light of all other clauses. Cal. Civ. Code section 1641.

> Where two clauses of an agreement appear to be in direct

> conflict, it is the duty of the court to reconcile such clauses so as to give effect to the whole instrument . . . . In so construing an agreement no term shall be considered uncertain or ambiguous if its meaning can be ascertained by fair inference from the terms of the agreement.

In re Marriage of Whitney, 71 Cal. App. 3d 179, 182-183 (1977) (citations omitted).

A court should

> adopt that construction which will make the contract reasonable, fair and just . . . ; should give it such interpretation "as will make it lawful, operative, definite, reasonable, and capable of being carried into effect, if it can be done without violating the intention of the parties" (Civ. Code Section 1643); should avoid an interpretation which will make the contract unusual, extraordinary, harsh, unjust, or inequitable . . . ; or which would result in an absurdity . . . ; and should reject language which is wholly inconsistent with its object . . . .

Harris v. Klure, 205 Cal. App. 2d 574, 577-578 (1962) (citations omitted).

Applying these general principles of contract interpretation and construing the contract as a whole, it is evident that the parties did not intend to contract away to the Districts all of the City's rights to local water in Lake Hodges. Paragraph 5 of the agreement sets forth the conditions under which the City may sell local water to any person, firm, corporation, or agency. According to the first condition, the City may sell water to another party if there is local water in Lake Hodges in excess of the quantity the City is required to furnish to the Districts for the remainder of the water year. Paragraph 7 of the 1969 Agreement establishes the amount of local water the City must furnish to the Districts. Consequently, at least 20,000 acre feet of local water per each "ten-year period" of the agreement must be available to the Districts. Pursuant to Paragraph 7, the Districts on average have requested 2,000 acre feet of local water per year. Thus, in accordance with the first condition the City may sell local water to any other person,

firm, corporation, or agency if it has local water in Lake Hodges in excess of the 2,000 acre feet of local water it is required to provide the Districts during the year in which the sale is to be made.

Pursuant to the second condition, the City may sell local water from Lake Hodges to another person, firm, corporation, or agency, if the City maintains in storage at least 8,300 acre feet of usable water in Lake Hodges for the exclusive use of the Districts. Significantly, this condition does not require 8,300 acre feet of "local water" to be stored in Lake Hodges for the Districts. The second condition must be read in light of the provisions of Paragraph 8. Paragraph 8 requires the City to provide the Districts, upon request, a total quantity of 7,500 acre feet of usable local or imported water. It is the understanding of our office from information provided by your department that 8,300 acre feet approximates the total amount of water the City must provide the Districts pursuant to Paragraph 8 (7,500 acre feet) plus the amount necessary to make up for water lost by evaporation in a given year.

As noted earlier, Mr. Cowett has concluded that Paragraph 8 provides the Districts with a guarantee of 7,500 acre feet of local water per year, if it is available. Mr. Cowett's conclusion, however, cannot be reconciled with the plain language contained in Paragraph 8, or with the second condition in Paragraph 5. Paragraph 8 provides that the City will provide the Districts with "a total quantity during each water year of 7,500 acre feet of local or imported water," in addition to the District's entitlement of water from the CWA. A fair inference can be drawn in reading these two paragraphs together that the City is guaranteeing to the Districts 7,500 acre feet of water which it may provide either from the local water collected at Lake Hodges or from its own allotment of water provided by the CWA. In either case, the City may sell its local water in Lake Hodges as long as it maintains the 8,300 acre feet of usable water in storage at Lake Hodges at the end of the water year.

This interpretation of the 1969 Agreement is further supported by Paragraph 17. This paragraph provides in relevant part that:

> the right of the Districts to purchase 7,500 acre feet of water from San Diego each year over and above their entitlements for water from the CWA, and the obligation of San Diego to furnish said water, is a property right . . . and said right is . . . a perpetual right vested in the

> Districts. All other provisions of
> this agreement shall expire September
> 30, 2019.

(Emphasis added.)

Again, the plain language of this provision of the contract does not specifically refer to the Districts having a right to 7,500 acre feet of "local water." Nowhere in the agreement is there a provision which requires that the provision of 7,500 acre feet be allotted first from the local water collected at Lake Hodges, and second from imported water if the local water is not available.

Moreover, it is clear that the parties intended that if imported water was sold by the City to the Districts that they would pay imported water prices. Paragraph 10 of the 1969 Agreement provides that the "Districts will pay for imported water furnished by San Diego to Districts at a rate established by the CWA . . . in effect at the time of delivery." It further provides that in the event that during any given ten-year period of the agreement the City is unable to provide at least 20,000 acre feet of local water to the Districts, then the City must provide them with an amount of imported water (at local water rates as defined in the agreement) to equal the deficiency. Construing the contract as a whole, if the parties intended that the 7,500 feet of water be provided first from local water, then certainly there would have been the same contingency in Paragraph 8 for providing imported water at local water rates as there is in Paragraph 10 for the 20,000 acre feet allotment.

The final condition of Paragraph 5 provides that the City may sell local water to any other person firm, corporation, or agency if it is put to beneficial use by the purchaser. This condition is easily satisfied if the City sells the water or uses it for itself.

As noted earlier, Mr. Cowett reads paragraphs 5, 7, and 8 of the 1969 Agreement as prohibiting the City from selling local water from Lake Hodges to any other party prior to meeting its obligation to the Districts. He interprets this obligation to be 20,000 acre feet of local water over a ten-year period and 7,500 acre feet of local water per year. It would appear from Mr. Cowett's interpretation of the 1969 Agreement that the only time the 7,500 acre feet of water would come from imported water would be if 7,500 acre feet of local water is not available in Lake Hodges in a given year. "An interpretation which gives a reasonable, lawful, and effective meaning to all the terms of a contract is preferred to an interpretation which leaves a part unreasonable, unlawful or of no effect." Rest. 2d Contracts Section 203(a). Mr. Cowett's interpretation of Paragraph 8 gives

no effect to the language "local water or imported water," and therefore should be rejected.

"Where a contract admits of two constructions, the court ought to adopt that which is most equitable and which will not give an unconscionable advantage to one party over the other." Brawner v. Wilson, 126 Cal. App. 2d 381, 385 (1954) (citing Southern Surety Co. v. Bank of Lassen County, 118 Cal. App. 149, 154 (1931)). Reviewing the 1969 Agreement in its entirety, it is clear that the City is obligated to provide the Districts 20,000 acre feet of local water during each ten-year period of the agreement. To conclude, however, that the City also must provide 7,500 acre feet of local water each year to the Districts reads far too much into the agreement, is contrary to the clear language of the agreement, and cannot be reconciled with the remaining clauses of the agreement. Moreover, such an interpretation would give the Districts an unconscionable advantage over the City by in effect depriving it of all use of its own resource (local water).

II. INTERPRETATION OF THE AGREEMENT BY THE PARTIES

Another fundamental canon of contract interpretation is that "the conduct of the parties subsequent to the agreement's execution should be considered in interpreting the parties' understanding of their respective commitments." United States Liab. Ins. Co. v. Haidinger-Hayes, Inc., 263 Cal. App. 2d 531, 538 (1968); accord Lemm v. Stillwater Land & Cattle Co., 217 Cal. 474, 481 (1933). "Parties are far less liable to have been mistaken as to the intention of their contract during the period while harmonious and practical construction reflects that intention, than they are when subsequent differences have impelled them to resort to law . . . ." Cutter Laboratories, Inc. v. Twining, 221 Cal. App. 2d 302, 312 (1963) (quoting Bohman v. Berg, 54 Cal. 2d 787, 795-796 (1960)). This general rule of contract interpretation is tempered by the additional rule that the interpretation given to a contract by the parties "may be considered only when the acts of the parties were positive and deliberate and done in attempted compliance with the terms of the agreement." U.S. Liab. Ins. Co., 263 Cal. App. 2d at 538 (quoting 12 Cal. Jr. 2d, Contracts, Section 130, p. 343).

Applying this principle to the instant case, it is clear that the parties in the past have construed the 1969 Agreement in a manner contrary to the interpretation now given by Mr. Cowett. You have provided to our office a document entitled "Summary of Contract to Purchase Lake Hodges Water Among City of San Diego, San Dieguito Water District and Santa Fe Irrigation District." (A copy of this document is attached as Exhibit D for your reference.) This document is not dated but apparently was

drafted in concert by representatives of the City and the Districts, prior to this dispute arising, to summarize their understanding of the 1969 Agreement. After reviewing the agreement the parties mutually agreed that in addition to the Districts' entitlement of water from CWA, the Districts have the right to purchase 7,500 acre feet of water per year from the City's entitlement of CWA water. There is no statement in this document demonstrating that the parties understood this 7,500 acre feet of water to be an entitlement to 7,500 acre feet of local water from Lake Hodges.

The parties further concluded that the City may use water from Lake Hodges or sell it to others if it leaves a quantity of water in Lake Hodges for the Districts' use for the balance of that water year plus 8,300 acre feet of water for the Districts for the following year. Again, the parties did not specify that the 8,300 acre feet of water must be "local water."

Paragraph 19 of the 1969 Agreement provides that "each party to this agreement agrees to execute such further documents as may be necessary to carry out the purposes and intent hereof." Arguably the document executed by the parties setting forth their understanding of the agreement falls within the purview of Paragraph 19, and therefore can be used to establish the intent of the parties.

From the foregoing it is evident that at a time when the parties were harmonious and were attempting to give a practical interpretation to the 1969 Agreement, they agreed that the Districts had a right to purchase 7,500 acre feet of water from the City's entitlement of CWA water. Notably, they did not state that the right to 7,500 acre feet of water is a right to 7,500 acre feet of local water. Additionally, the parties agreed that the City may sell or use local water as long as the Districts' water needs were protected. These needs may be served by providing either local water or imported water.

Conclusion

In summary, we believe the rights of the City and the Districts pursuant to the 1969 Agreement are as follows:

(1) The Districts are entitled to 20,000 acre feet of local water during each ten-year period of the 1969 Agreement.

(2) The Districts have a perpetual property right to 7,500 acre feet of local or imported water from the City.

(3) The City may use or sell to another party local water from Lake Hodges under certain conditions.

   (a) First, the City must retain sufficient local water in Lake Hodges to meet its

obligation under the agreement (20,000 acre feet per ten-year period, or 2,000 acre feet per year on average).

(b) Second, the City must retain at least 8,300 acre feet of usable water in Lake Hodges to meet the Districts' right to 7,500 acre feet of local or imported water per year.

(c) Finally, the local water being sold must be beneficially used.

This interpretation of the 1969 Agreement appears to conform to the operational assumptions of Lake Hodges that you forwarded to us.

We hope this information answers your questions regarding the 1969 Agreement. If you have any additional questions, please do not hesitate to contact our office.

JOHN W. WITT, City Attorney
By
Kelly J. Salt
Deputy City Attorney

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Attachments
ML-94-98