

Appendix D

WATER SUPPLY CONTRACTS AND AGREEMENTS

ORIGINAL

WOODINVILLE WATER DISTRICT
KING COUNTY WASHINGTON
RESOLUTION NO. 3512

A RESOLUTION of the Board of Commissioners of the Woodinville Water District, King County, Washington, approving the signing of the water supply contract between the City of Seattle and the Woodinville Water District.

WHEREAS, it is in the best interest of the Woodinville Water District and its' customers to enter into a long term relationship for the supply of potable water; and

WHEREAS, the City of Seattle is the current provider of potable water to the District; and

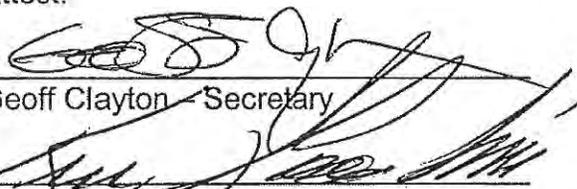
WHEREAS, the District's current contract with the City of Seattle expires in 2011; and

WHEREAS, the Woodinville Water District wishes to continue its relationship with the City of Seattle, **NOW THEREFORE**,

BE IT RESOLVED that the Board of Commissioners of the Woodinville Water District, King County, Washington enter into a new water supply agreement with the City of Seattle to provide potable water to the District.

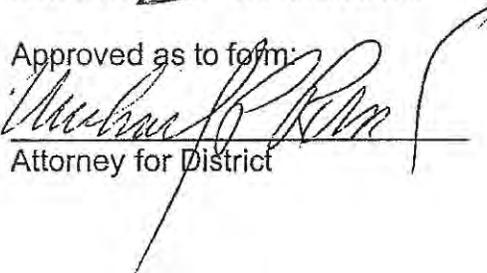
ADOPTED by the Board of Commissioners of the Woodinville Water District, King County, Washington at a regular Board meeting thereof this 7th day of December, 2004.

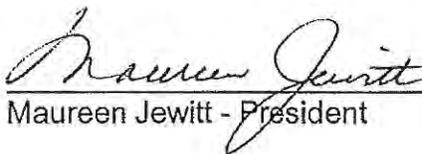
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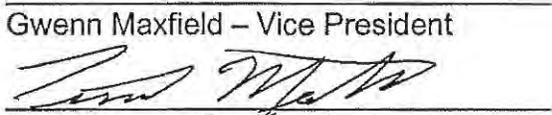

Geoff Clayton - Secretary


Ken Goodwin - Commissioner

Approved as to form:


Attorney for District


Maureen Jewitt - President


Gwenn Maxfield - Vice President


Tim Matson - Commissioner

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CITY OF SEATTLE
FULL REQUIREMENTS CONTRACT
FOR THE
SUPPLY OF WATER
TO
WOODINVILLE WATER DISTRICT

11/30/04

ORIGINAL

TABLE OF CONTENTS

	<u>Page(s)</u>
SECTION I. DEFINITIONS	2
SECTION II. TERM OF CONTRACT AND GUARANTEES	3
II.A. TERM OF CONTRACT.....	3
II.B. AGREEMENT TO SUPPLY AND PURCHASE WATER.....	4
II.C. CONTINUITY OF SERVICE WITHIN THE TERM OF THE CONTRACT	6
II.D. WATER QUALITY.....	7
II.E. CONSERVATION.....	8
SECTION III. CONDITIONS OF SERVICE.....	9
III.A. MINIMUM HYDRAULIC GRADIENT.....	9
III.B. REALE TO OTHER PARTIES	10
III.C. INTERCONNECTION WITH OTHER SYSTEMS.....	10
III.D. DEVELOPMENT OF REGIONAL SUPPLY AND TRANSMISSION INFRASTRUCTURE.....	11
III.E. METERING EQUIPMENT	11
SECTION IV. COST OF WATER & TRANSMISSION	12
IV.A. RATE-MAKING PRINCIPLES.....	12
IV.B. RATEMAKING FRAMEWORK	13
IV.C. WATER SUPPLY PRICING – BASIC SERVICES	13
IV.D. TRANSMISSION PRICING - BASIC SERVICES.....	15
IV.E. ALLOCATION OF COSTS AND REVENUES INTO COST POOLS	16
IV.F. ELECTIVE SERVICES	23
IV.G. RATE ADJUSTMENT	23
IV.H. RETAIL RATE-SETTING.....	24
IV.I. TRUING ACTUAL COSTS AND ACTUAL REVENUES	24
SECTION V. OPERATING BOARD	24
SECTION VI. PLANNING	25
VI.A. REPORTING OF PLANNING DATA	25
VI.B. SUBMITTAL OF WATER UTILITY COMPREHENSIVE PLANS.....	25
VI.C. SEATTLE AS WATER PLANNING AGENCY.....	25
VI.D. COMPREHENSIVE CAPITAL FACILITIES PLAN.....	26
VI.E. EMERGENCY PLANNING	26
SECTION VII. PAYMENT	26
VII.A. COLLECTION OF MONEY DUE CITY	26
VII.B. PENALTIES FOR LATE PAYMENT.....	26
VII.C. DISPUTES.....	26
SECTION VIII. CONTRACT AMENDMENTS.....	27
SECTION IX. DISPUTE RESOLUTION.....	27
IX.A. OPERATING BOARD REVIEW	27
IX.B. SEATTLE CITY COUNCIL REVIEW	27
IX.C. NON-BINDING MEDIATION	28
IX.D. RESORT TO LITIGATION.....	28

TABLE OF CONTENTS

(cont.)

SECTION X. MISCELLANEOUS.....	28
X.A. NOTIFICATION.....	28
X.B. SEVERABILITY.....	28
X.C. CONSENT.....	29
X.D. EMERGENCY SITUATIONS.....	29
X.E. NO JOINT VENTURE - INDIVIDUAL LIABILITY.....	29
X.F. COMPLETE AGREEMENT.....	29
X.G. RELINQUISHMENT OF PRIOR CONTRACT.....	29
X.H. VENUE, JURISDICTION AND SPECIFIC PERFORMANCE.....	30
X.I. DEFAULT.....	30
X.J. FORCE MAJEUR.....	30
X.K. SUCCESSORS.....	30
X.L. EXHIBITS.....	30

**FULL REQUIREMENTS CONTRACT
BETWEEN
THE CITY OF SEATTLE
AND
WOODINVILLE WATER DISTRICT
FOR THE SUPPLY OF WATER**

THIS CONTRACT is entered into between the CITY OF SEATTLE ("Seattle"), a municipal corporation of the State of Washington, and WOODINVILLE WATER DISTRICT ("Woodinville"), a municipal corporation of the State of Washington.

RECITALS

1. Seattle owns and operates a system for the supply, transmission and distribution of potable water and is authorized to sell and distribute water to its residents and to other persons and customers located outside the corporate limits of Seattle.
2. Seattle's water system is integral to the health and welfare of the residents located within the water service area shown in Seattle's Water System Comprehensive Plan. Seattle intends to provide water from the system to meet the current and future needs of the residents of such water service area when such service is requested from Seattle.
3. In meeting this service commitment, Seattle must ensure that this role does not place financial burdens on its retail customers for which they do not receive a corresponding benefit.
4. This contract and contracts of a similar nature with other wholesale customers of Seattle located within Seattle's service area are intended to provide those customers with the security of a long term service commitment and to describe the terms and conditions associated with that commitment.
5. Under this contract, Seattle intends to provide wholesale water to Woodinville at an equivalent level of service and under the same pricing principles as it provides water to Seattle's own distribution system.
6. Given the extensive of growth of the Seattle and surrounding areas and the impacts upon infrastructure and costs, this contract is intended to provide sufficient water for growth. As a general philosophy for cost sharing purposes, the parties desire to adopt the principle that "growth should pay for growth."
7. Seattle and Woodinville, together with other wholesale customers of Seattle, have agreed to establish an Operating Board comprised of representatives pledged to represent the best interests of the region in order to provide overall direction to the Administrator of the Seattle Water Supply System.

NOW, THEREFORE, in consideration of mutual covenants herein, it is agreed as follows:

SECTION I. DEFINITIONS

For the purposes of this contract, the following terms have been defined as:

"Full Water Requirements" - All of the water needed by Woodinville to meet the needs of its present and future water customers within its service area as shown in Woodinville's comprehensive water system plan.

"Block Purchase Contract" - A contract in which Seattle sells a fixed quantity of water to the Wholesale Customer on a take or pay basis.

"Full Requirements Contract" - A contract in which Seattle supplies a Wholesale Customer with its Full Water Requirements.

"Partial Requirements Contract" - A contract in which Seattle supplies a Wholesale Customer with that portion of its Full Water Requirements above that provided by the Wholesale Customer's own supply.

"Wholesale Customer" - Those customers who receive water from Seattle for the purposes of reselling to others.

"1982 Water Purveyor Contract" - That certain Water Purveyor Contract between Woodinville and Seattle having an effective date of September 8, 1982.

"Existing Supply Resources" - Current components of the Seattle Water Supply System which consist of the Cedar River storage, treatment and diversion facilities, the Tolt River storage, treatment and diversion facilities, and the Highline Well Field as set forth in Exhibit VII.

"FC" - Means Facility Charge.

"FC Waiver Event" - A reasonably unforeseeable interruption of a source of supply operated by Woodinville that lasts for more than three weeks and is cured within two calendar years, including but not limited to major pump failure, earthquake and water quality problems.

"1% Water Conservation Program" - A program which has been implemented by Seattle with the agreement of Woodinville which contains a goal of 1% conservation per year for ten years.

"Seattle Water Supply System" - Seattle's water supply system consisting of dams, impounded water, supply and transmission mains, pumps, treatment facilities, and all other facilities utilized in conveying water to Seattle's retail service area, to Woodinville and other Wholesale Customers. This definition does not include Seattle's water distribution system, which is used to serve its Retail Customers.

"Seattle's Average Cost of Debt" - The weighted average interest rate on Seattle's water system debt outstanding calculated at the end of each calendar year during the term of this contract.

"Rate of Return on Investment" - Seattle's Average Cost of Debt, plus 1.5 percent.

"Service Connection" - The water meter and appurtenances through which water is delivered from the Seattle Water Supply System to a Wholesale Customer's water system.

"Seattle Transmission Facilities" - Those facilities serving Seattle's regional transmission needs as set forth in Exhibit VIII.

"Stranded Costs" - Those water supply and related costs that Seattle and others have invested for the region that may not be recovered as a result of lost revenues.

"Seattle Water System Comprehensive Plan" - Seattle's Water System Comprehensive Plan dated April, 2001, and amendments thereto, prepared by Seattle to comply with the requirements of WAC 248-54-580, and successor regulations.

"System-wide Average Annual Residential Use" - The average, considering all Wholesale Customers and Seattle's retail customers, of the annual demand of a single-family residential customer.

"Administrator" - The Director of Seattle Public Utilities or any other title given to that person who maintains the authority to operate and manage the Seattle Water Supply System.

"Operating Board" - A board of representatives having the powers and duties set forth in Section V hereof.

SECTION II. TERM OF CONTRACT AND GUARANTEES

II.A. Term of Contract

1. Term. This contract shall take effect upon the signature of both parties and shall remain in effect until 12:01 AM on January 1, 2062.
2. Subsequent Right Of First Refusal. At the end of the term of this contract, Woodinville shall have a right of first refusal to continue to purchase the amount of water then purchased from Seattle at the time of contract expiration.
3. Periodic Review and Right to Change Certain Terms and Conditions. The parties may review and change certain terms and conditions governing the sales of water hereunder on January 1, 2022 and January 1, 2042 as follows.
 - a. Consensual Process. On or before January 1, 2021, and then again on or before January 1, 2041, either party may provide the other with a written proposal to amend the contract terms. The parties shall then meet and consider the proposal. If the parties agree to the proposal prior to January 1, 2022 and January 1, 2042, respectively, a written amendment to this contract shall be approved and executed by both parties and this contract shall be amended accordingly.

- b. Seattle's Right to Amend. If the parties are unable to agree on a proposal by Seattle pursuant to subsection a. above within the respective one-year periods, Seattle may propose in writing its desired amendment to the Operating Board. Seattle and the Operating Board shall meet and consider the proposed amendment and use reasonable efforts to resolve any differences in the proposal. After 90 days from Seattle's written proposal to the Board, Seattle may propose its desired amendment to the Seattle City Council. If the Operating Board does not agree with such proposal, it may submit a revised proposal to the Seattle City Council within 90 days of Seattle's submission of its proposal to the Seattle City Council. After receiving the Operating Board's alternate proposal, or after the lapse of the 90 day period for the Operating Board to make an alternate proposal, the Seattle City Council may then deny both proposals or approve one of them and issue an amendment to this contract which shall be in effect for the remaining term of the contract from the date of issuance, unless later amended pursuant to subsection a. above, or by mutual agreement.
- c. Limitation on Seattle's Right to Amend. Notwithstanding subsection b. above, Seattle shall not have the right to: (i) reduce its obligation to provide the Full or Partial Water Requirements of Woodinville; (ii) cease to provide wholesale water to Woodinville at an equivalent level of service as it provides water to Seattle's own distribution system. (iii) charge a higher wholesale rate for water supply and transmission to Woodinville than that charged to Seattle for supply to its retail customers, (iv) reduce its water quality obligations hereunder, (v) change the methodology for calculating Rate of Return on Investment, (vi) restrict Woodinville's right to withdraw from this contract, and (vii) disband or significantly reduce the powers of the Operating Board.

II.B. Agreement to Supply and Purchase Water

1. Full Requirements Commitment. Seattle shall provide sufficient water supply to meet Woodinville's full water requirements during the term of this Agreement; provided that if a reduction in purchase commitment occurs as set forth in section II.B.5 below, Seattle shall thereafter supplement Woodinville's independent sources as identified in Exhibit X and as set forth in Exhibit I. Subsequent to the establishment of the quantities available from its independent sources, Woodinville may purchase its remaining, supplemental wholesale water needs from Seattle according to the terms of this Agreement. Provided further that should Woodinville lose its independent sources, Seattle's full requirements commitment shall be maintained pursuant to this Agreement provided that Woodinville has purchased at least 100 million gallons of water each year from Seattle under this Agreement.
2. Adjustments in Woodinville's Service Area. In the event Woodinville acquires additional service area that is: 1) located outside of the service area identified in its comprehensive water system plan and 2) which is not already served with Seattle water, then Seattle shall supply the water requirements of the additional service area subject to a) Seattle's ability to serve that area, and b) Woodinville's payment of FCs for that additional service area in accordance with section IV.E.

3. Assumption or Transfer of Responsibilities. In the event Woodinville's entire service area and service responsibilities are assumed by or are transferred to another utility, then this contract shall become null and void at the time of the assumption or transfer; provided, however, if the transferee of the service area is a Wholesale Customer, Seattle shall provide water to the transferee according to the terms of the transferee's water supply contract with Seattle. If the transferee is not a Wholesale Customer, then Seattle shall issue the transferee a water supply contract for such area subject to terms and conditions as Seattle shall determine.
4. Annexation by Seattle. If the entire water service area of Woodinville is annexed to Seattle, then this contract shall become null and void upon Seattle's assumption of Woodinville's water system.
5. Woodinville's Right to Terminate or Reduce Purchase Commitment. Woodinville's commitment to purchase water from Seattle under this contract may be terminated or reduced subject to the terms and conditions set forth below. Woodinville shall provide Seattle at least 5 years written notice thereof, provided, however, if Seattle unilaterally amends the terms and conditions of this contract pursuant to Section II.A.3 above, Woodinville may terminate this contract at any time within 1 year thereafter by giving Seattle 1 year written notice.
 - a. Automatically Permitted Reductions. Woodinville may, with each reduction request, and without restriction, upon five years written notice to Seattle, reduce its water purchases from Seattle by an amount not to exceed 10 million gallons per day of its average annual demand, *provided*, that such notice of water purchase reduction may be given to Seattle no more than once every five years, and that the reduction in water purchases by Woodinville may not exceed 10 million gallons per day of its average annual demand in any consecutive five year period.
 - b. Reductions Requiring Permission. Woodinville may reduce quantities of water purchased from Seattle by more than the amount identified in the preceding section or by providing less than five years advance notice of such reduction if Woodinville in the judgment of the Operating Board, using the criteria listed below it determines that such reduction is in the best interest of the Seattle Water Supply System as a whole.
 - c. Criteria. The criteria to be used by the Operating Board in determining the best interest of the Seattle Water Supply System shall include but not be limited to the following:
 - i. The potential for Stranded Costs and impacts on rates;
 - ii. The cost of new resources;
 - iii. The feasibility and benefit of reallocating to Seattle or other customers the amount of water foregone by Woodinville; and
 - iv. Environmental aspects of the proposed change.

The Operating Board shall act promptly and reasonably in evaluating and deciding upon Woodinville's request. The Operating Board may approve, with or without reasonable conditions, or deny Woodinville's request based on the above criteria. Approval conditions may include a requirement that Woodinville waive its rights to be served its Full Water Requirements. If the approval conditions are unacceptable to Woodinville it may elect in writing to withdraw its request and this contract shall continue in full force and effect.

II.C. Continuity of Service within the Term of the Contract

1. Parity of Service. Seattle shall provide wholesale water to Woodinville at an equivalent level of service that it provides to Seattle's own distribution system. In the event of a general emergency or weather-related water shortage affecting the entire Seattle Water Supply System, general restrictions placed upon water deliveries to Woodinville shall be determined by the Operating Board and applied equally to Seattle's distribution system and the Wholesale Customers. In the event of localized emergency problems, Woodinville acknowledges temporary, localized service interruptions may occur for the duration of the emergency.
2. Emergency Curtailment Measures. It is recognized by both parties that emergency water use curtailment measures may have to be implemented by Seattle on a regional basis in order to meet an emergency condition or a regional water shortage. The procedures to be used in the event of a weather-related regional water shortage, or shortages caused by other factors, shall be as described in Seattle's Water Shortage Contingency Plan in effect as of the effective date of this contract, or successor contingency plans. Successor contingency plans shall be developed and implemented by Seattle in consultation with the Operating Board. Woodinville shall assist with and support all emergency curtailment measures that are implemented.
3. Other Emergencies. Seattle may temporarily interrupt or reduce deliveries of water to Woodinville if Seattle determines that such interruption or reduction is necessary or reasonable in case of system emergencies or in order to install equipment, make repairs, replacements, investigations and inspections or perform other maintenance work on the Seattle Water Supply System. Except in cases of emergency, and in order that Woodinville's operations will not be unreasonably interrupted, Seattle shall give Woodinville and the Operating Board reasonable notice of any such interruption or reduction, the reasons for and the probable duration. Seattle shall use its best efforts to minimize service interruptions to Woodinville.
4. Waiver Of Charges. If interruption or reduction in service to Woodinville requires that Woodinville draw water supply in a manner that subjects Woodinville to demand charges (as described in Exhibit III hereto), Seattle shall waive such charges during the period of such interruption or reduction.

II.D. Water Quality

1. Seattle Water Supply System. Seattle shall be responsible for water quality within the Seattle Water Supply System as set forth below. Seattle shall construct, operate and maintain water quality treatment facilities and use its best efforts to carry out its water quality responsibilities in the most cost-effective manner for the region.
2. Applicable Standards. Seattle shall at all times during the term hereof deliver water to Woodinville's system that meets or exceeds all applicable Federal, State and local regulations as the same may change from time to time.
3. System-wide Water Quality Plan. Seattle, in consultation with the Operating Board, shall develop and maintain a system-wide regional water quality plan. The plan shall describe, at a minimum, goals, objectives, procedures and the means to satisfy legal requirements and industry standards for water quality, monitoring, information exchange, best management practices, adaptive management practices, public health protection, and cross connection control. The Operating Board may form a technical subcommittee to provide input and review of such plan. Seattle shall share available water quality data and technical expertise with all Wholesale Customers.
4. Distribution Systems. Woodinville shall be responsible for compliance with all applicable federal, State and local water quality laws and regulations applicable to water in its distribution system including any water from supply sources that it may own or operate.
5. Monitoring. Water quality monitoring shall be performed by Seattle in the Seattle Water Supply System and by Woodinville in its distribution system to comply with federal, State and local water quality regulations, to verify the condition of water that is passing from one entity to the other, to enhance system operation and to document the aesthetic qualities of the water. Notwithstanding the foregoing, Woodinville may contract with Seattle for water quality monitoring services as an elective service under Section IV.F. hereof.
6. Water Quality Notifications to Customers (Consumer Confidence Reports). Each party shall prepare at its sole cost periodic water quality notifications to its respective retail customers and regulatory agencies as required by law. Seattle shall provide Woodinville all water quality data in a timely manner regarding the Seattle Water Supply System that Woodinville may be legally required to report in such notices.
7. Water Quality Best Management Practices and Adaptive Management Practices. The Operating Board shall develop best management practices ("BMPs") and adaptive management practices ("AMPs") as reasonably necessary to protect water quality within the Seattle Water Supply System. The BMPs and AMPs will include recommendations to prevent deterioration of water quality in transmission and distribution systems. The parties shall use reasonable efforts to comply with the BMPs and AMPs.

8. Flushing. Woodinville shall be solely responsible for flushing water mains within its system. Flushing allowances will be provided by Seattle only when the Operating Board determines that flushing is required to maintain or improve regional water quality.
9. New Water Sources. Prior to the introduction of any new water supply source that Woodinville mixes with water in Seattle's Transmission Facilities, the proposed source must be evaluated using customary and reasonable water quality criteria developed in consultation with the Operating Board to ensure compatibility with Seattle water. The proposed Woodinville source must also meet all federal, state and Seattle water quality and treatment standards. Woodinville shall also provide Seattle, if requested, with satisfactory results from a blending study to determine the compatibility of the source with existing sources already in the Transmission System, the appropriate method and level of treatment and the probable distribution of the new supply within the Transmission System. Woodinville shall also complete a flavor rating analysis of no more than 3.0 as tested by Seattle's Flavor Profile Panel according to the methodology described by the American Water Works Association, or its successor. Woodinville shall obtain all necessary and appropriate regulatory permits, reviews and approvals for rights to and operational use of such water supply source. The introduction of any direct or indirect potable reuse water into Seattle's Transmission Facilities shall, in addition, require Seattle's prior written consent.

The Operating Board may form a technical subcommittee to develop water quality standards and review and advise on the water quality evaluation criteria for proposed new sources. Such criteria for new sources shall be the same for surface water and ground water.

10. Transfers Outside Seattle's Transmission System. If, with the consent of Seattle, Seattle's water is transferred between Woodinville and another water utility in a manner that does not use the Seattle Water Supply System, Woodinville or the other water utility shall be responsible for meeting all applicable water quality standards related to the transfer of such water.

II.E. Conservation

The parties acknowledge that conservation prolongs the time before new supply resources are needed and thus constitutes an important ongoing tool in managing the water resources of the region. Accordingly, Woodinville hereby adopts and agrees to be bound by Seattle's 1% Water Conservation Program through the year 2010.

1. Performance Measurements. For the purposes of determining water conservation performance, Woodinville's water use shall be measured in conjunction with the use of all other participants in Seattle's 1% Water Conservation Program. The Operating Board may develop reasonable criteria to measure the participants' water conservation performance in accordance with such program.

2. Conservation Above the 1% Program. Woodinville acknowledges that water conservation beyond the 1% Water Conservation Program may be required as condition of State or federal regulations, court orders, settlements or agreements made to avoid litigation, fines or penalties, or as otherwise determined to be reasonably necessary by the Operating Board. The Operating Board may adopt reasonable additional conservation measures and targets for such purposes. Such conservation measures and targets shall apply in the same manner to all holders of Full and Partial Requirements contracts and to Seattle. Except as provided in the next subsection, Woodinville shall use reasonable efforts to abide by and perform such water conservation measures and to meet the adopted targets.
3. Woodinville's Option to be Conservation Service Provider. Woodinville may elect to provide its own water conservation program, beyond its commitment to the 1% Water Conservation Program to meet conservation targets adopted by the Operating Board or more stringent targets. Woodinville shall bear the costs thereof and shall be solely responsible for its implementation. Under this option, Woodinville shall be evaluated for meeting water conservation targets solely by its own performance.
4. Incentives and Penalties. The Operating Board may adopt penalties for shortfalls in water conservation and rewards for meeting or exceeding adopted targets. In the event Woodinville fails to meet the adopted targets set by the Operating Board, the Operating Board may assess a penalty. Penalties may not exceed the cost of Seattle undertaking those conservation measures reasonably needed to achieve the adopted target.
5. Postponing The Need For New Water Supply Facilities. In order to avoid the necessity of developing new physical water supply facilities for as long as reasonably practicable, any water saved through conservation in either Seattle's or Woodinville's retail service areas shall be dedicated first to the municipal and industrial water supply requirements of the Seattle Water Supply System before any other use of such water may be undertaken.

SECTION III. CONDITIONS OF SERVICE

III.A. Minimum Hydraulic Gradient

1. Initial Minimum. Seattle shall maintain a minimum hydraulic gradient or head at a maximum flow rate in amounts and at locations described in Exhibit II attached hereto for each Service Connection from Seattle's Water Supply System to Woodinville's distribution system. Such gradients and locations shall be contained in Seattle's and Woodinville's future water system comprehensive plans. Seattle shall operate and maintain facilities necessary to carry out such obligation. If Seattle and the Operating Board find that a project resulting in the modification of such minimum gradient or head would benefit the Seattle Water Supply System as a whole, the minimum hydraulic gradient or head described in Exhibit II may be modified by Seattle if such modification is feasible from an economic, land use and engineering perspective taking into account the facilities required to carry out and for Water Utility to adapt to such modification. Seattle may make these modifications only once during any fifteen (15) year period provided that four (4) years advance written notice is given to Woodinville, unless the Operating Board approves a shorter notice.

2. Emergencies. If Seattle is prevented by emergency circumstances from providing such minimum hydraulic gradient, Seattle shall supply not less than the volume of water equivalent to the maximum 24-hour average flow rate required by Woodinville as shown on Exhibit II for each 24 hour period that the minimum hydraulic gradient is interrupted.
3. Additional Service Connections. Additional Service Connections between Woodinville's and Seattle's water systems or adjusted minimum gradients may be established from time to time by mutual agreement between Seattle and Woodinville subject to approval by the Operating Board. Exhibit II shall be appropriately amended to reflect such additions or adjustments.

III.B. Resale to Other Parties

Woodinville may sell the water it develops and/or acquires independently of Seattle to other utilities located outside of Woodinville's existing service area boundaries subject to appropriate modification of Woodinville's Water System Plan and approval by the Washington State Department of Health.

Woodinville may sell water supplied by Seattle to water purveyors located outside of Woodinville's existing or future boundaries only upon the prior written consent of Seattle (or oral, in case of emergency). Agreements for resale of water by Woodinville listed in Exhibit I are hereby approved by Seattle subject to whatever written terms, conditions and limitations that Seattle has imposed on such resale.

III.C. Interconnection With Other Systems

1. Prohibition on Interconnection. Woodinville shall not interconnect any part of its system supplied with water from Seattle with other water systems without the prior written approval of the Operating Board, or, in case of emergency, upon oral approval by Seattle, which shall not be unreasonably withheld. Any such interconnection shall be subject to the approval of the Washington State Department of Health and the installation of a meter. Such other systems must be in compliance with all applicable local, State and federal laws and regulations including the requirement that they have a valid operating permit issued by the Washington State Department of Health.
2. Requests by Seattle to Interconnect. Seattle may request that Woodinville interconnect its water system to the water system of an adjacent Wholesale Customer. Woodinville shall comply with that request subject to the terms and conditions set forth below.
3. Requirement for Interconnection. If Woodinville does not consent to Seattle's request for interconnection, Seattle may propose the interconnection of Woodinville's water system to the adjacent Wholesale Customer to the Operating Board. Woodinville may present facts and arguments to the Operating Board in opposition to the interconnection and/or to document its costs in making the interconnection and conveying water to the adjacent Wholesale

Customer. The Operating Board shall hear and consider the matter. Upon (a) a written finding by the Operating Board that the proposed interconnection with an adjacent Wholesale Customer is feasible taking into account Woodinville's capabilities, limitations and obligations, (b) a written finding by the Operating Board that such interconnection benefits the Seattle Water Supply System and (c) a written demand of the Operating Board that Woodinville carry out the interconnection, Woodinville shall be required to interconnect its facilities to the adjacent Wholesale Customer for the purpose of supplying water to that Wholesale Customer through the distribution system of Woodinville, provided that the interconnection shall be performed in a location and according to a schedule which does not unduly disrupt Woodinville's operations.

4. Payment and Indemnity. Woodinville shall be paid by Seattle for its actual costs of providing such interconnection and water transmission service to the adjacent Wholesale Customer, plus a reasonable amount for overhead, administration and rate of return (equal to Rate of Return on Investment) on such costs, and Woodinville shall be indemnified by Seattle from any liability that may result from providing such interconnection. Further, as indemnitor, Seattle shall provide and pay for the defense involving said liability. The Operating Board shall adopt a standard methodology for calculating costs that ensures that Woodinville is fairly compensated for such service.

III.D. Development of Regional Supply and Transmission Infrastructure

1. Final decisions and authority to approve construction of capital infrastructure related to the Seattle Water Supply System shall rest with the Seattle City Council. Capital construction activities include all renewals, replacements, upgrades, expansion and any other capital construction activities.
2. Nothing herein shall restrict Woodinville's authority to:
 - a. construct an independent water transmission system for its own water supply; or
 - b. develop and/or acquire additional independent supply source(s) that may use Woodinville's distribution system and/or independently constructed transmission system.

III.E. Metering Equipment

Seattle shall own and maintain appropriate metering devices to measure the amount of water delivered to Woodinville pursuant to this contract. At Woodinville's request and expense, Seattle shall install and maintain equipment selected by Woodinville and approved by Seattle to transmit signals to Woodinville's recording equipment (at locations determined by Woodinville) of the amount of water delivered as measured by Seattle's meter(s).

Until such time as Seattle determines it to be economical to install metering devices to measure the amount of water delivered from the Seattle Water Supply System to Seattle's distribution system, the amount of water delivered to the Seattle distribution system shall be measured indirectly by subtracting the metered water delivered to all of Seattle's Wholesale Customers

from 98% of the total amount of water exiting Seattle's sources of supply as measured by the supply meters.

SECTION IV. COST OF WATER & TRANSMISSION

Cost-based rates are a water industry accepted practice and the historical practice of Seattle and the Wholesale Customers. The rate-making principles, policies and methodologies set forth in this Section IV are intended to meet the objective of equitable and cost-based rates.

IV.A. Rate-making Principles

The following general principles and policies shall apply to the establishment of all rates and charges for water supply and related services hereunder beginning on January 1, 2005. Prior to that date, the pricing method of the 1982 Water Purveyor Contract shall be maintained.

1. No expenses attributable to electric power development maybe allocated to the cost pools identified herein unless the pools are allocated a commensurate share of revenue derived from such development.
2. Seattle shall utilize generally accepted accounting principles consistently applied as a basis for developing the financial information upon which rates and charges are based.
3. Abrupt changes in financial policies should be avoided.
4. The rate structure should encourage the efficient use of water, conservation and the timely development of new environmentally responsible water sources and should incorporate seasonal rates and other pricing approaches to encourage efficient use.
5. The rate structure should be innovative, flexible and adaptive whenever it is cost effective and beneficial in furthering the rate making policies.
6. The rate structure should be simple to administer and easily understandable.
7. The rate structure should be fair and equitable while the balancing the needs of all parties.
8. Capital costs which benefit only a new Wholesale Customer shall be allocated to that customer and not to any cost pool described in this contract.
9. Seattle's distribution system which serves its retail customers shall be treated as the equivalent of a Wholesale Customer of the Seattle Water Supply System for the purpose of charging Seattle the same wholesale rates and charges as Woodinville for water supply and transmission. Costs calculated under the costs pools described below shall apply equally to Woodinville and to Seattle's distribution system, which serves its retail customers.

10. The allocation of costs associated with capital construction activities within the Seattle Water Supply System shall be the responsibility of the Operating Board. The Operating Board shall use its best efforts to determine and approve a cost allocation method for infrastructure projects prior to the capital project obtaining construction approval from the Seattle City Council. Failure of the Operating Board to determine and approve a cost allocation method shall not hinder the Seattle City Council from approving capital infrastructure projects in order to assure Seattle's ability to fulfill the requirements of this contract.
11. The purveyor balance account as that term is defined in the 1982 Water Purveyor Contract between Seattle and Woodinville shall be credited to the Wholesale Customers in a ratable and equitable manner commencing with the application of rate making policies and framework.

IV.B. Ratemaking Framework

Subject to the foregoing principles, wholesale rates and charges for the services described in this contract shall be developed by Seattle based on the following framework:

1. Water Supply and Transmission Service. The costs of water supply and transmission of water shall be accounted for separately in the water supply and transmission cost pools described below. The price for each service shall be recovered through separate rates for each service. All direct costs incurred in providing water supply and transmission services shall be allocated to the appropriate cost pool and recovered through the rates for each service. In addition, certain indirect costs consisting of a reasonable overhead and administration cost shall be allocated to the appropriate cost pool and recovered through rates for each service.
2. Water Supply - Basic and Elective Services. The costs of supplying water falls into two categories – basic and elective services. Basic service costs includes direct and indirect costs attributable to the delivery of water to the Wholesale Customers and to Seattle's retail service area pursuant to the foregoing principles. Elective services are optional services, such as water quality laboratory services and specific engineering support that Seattle makes available.
3. Conservation. Costs incurred by Seattle for regional conservation shall be accounted for in the New Supply Cost Pool and allocated to the Wholesale Customers through rates or FCs as determined by the Operating Board.

IV.C. Water Supply Pricing – Basic Services

1. Two Water Supply Cost Pools. For the purposes of determining costs of water supply, there shall be two cost pools: An existing supply cost pool ("Existing Supply Cost Pool") and a new supply cost pool ("New Supply Cost Pool").

- a. Existing Supply Cost Pool. The Existing Supply Cost Pool shall be accounted for as follows:
- i. A basic services rate for water supply shall be levied to recover the full costs of operating maintaining and replacing the Existing Supply Resources incurred by Seattle.
 - ii. All conservation programs undertaken by Seattle prior to the effective date of this contract with the exception of the costs of the 1% Program from January 1, 2002 through 2010, shall be considered an Existing Supply Resource cost.
 - iii. Renewal and replacement of Existing Supply Resources will be an Existing Supply Resource cost.
- b. New Supply Cost Pool. The New Supply Cost Pool shall be accounted for as follows:
- i. Water supply resources developed in the future ("New Supply Resources") that expand the capacity of the Seattle Water Supply System, including the costs of the 1% conservation program from January 1, 2002 through 2010, shall be included in the New Supply Cost Pool. If any portion of a New Supply Resource project enhances reliability of Existing Supply Resources, the costs thereof may be allocated to the Existing Supply Cost Pool if the Operating Board and Seattle both agree.
 - ii. The cost of New Supply Resources plus Rate of Return on Investment may be recovered through FCs charged annually to the holders of Full Requirements Contracts, Partial Requirements Contracts and Seattle or through new supply rates based on the costs of such facilities. Such costs, which are not recovered on an annual basis through FCs, shall be recovered through new supply rates. The new supply rate shall be applied to all holders of Full Requirements Contracts and Partial Requirements Contracts and Seattle. It is Seattle's policy and practice not to collect revenue to pay a cost in advance of incurring such cost. Seattle reserves the right to change this policy and practice in the future in consultation with the Operating Board.
 - iii. The Operating Board shall determine the portion of the New Supply Resource costs that shall be recovered through FCs or through new supply rates. The FCs and new supply rates may be scalable to create an incentive for developers to build housing or commercial units with efficient water usage levels. Water Utility, as well as each other Wholesale Customer and Seattle in setting rates for retail customers shall be free to choose the method of incorporating FCs or new supply rates into their own retail rates and charges.
 - iv. Holders of Full and Partial Requirements Contracts who have not purchased water from Seattle under the 1982 Water Purveyor Contract between Seattle and the Wholesale Customer shall be assessed the full marginal costs of the operation, including Rate of Return on Investment, of the New Supply Facilities. This

assessment may be satisfied by either paying FCs and new supply rates or arranging a special water supply rate in lieu of paying FCs.

- c. Emergency Surcharge. In the event of a drought, catastrophe or other extraordinary condition that requires emergency expenditures to maintain a sufficient water supply, Seattle may impose an emergency surcharge on all holders of Full and Partial Requirements Contracts in order to pay for such expenditures and/or maintain financial stability of the Seattle Water Supply System. Any such emergency surcharge shall be presented to the Operating Board prior to adoption by Seattle. Seattle shall consider the comments of the Operating Board but shall nevertheless have the full authority to adopt the charge.

IV.D. Transmission Pricing - Basic Services

- 1. Transmission Costs Pools. For purposes of determining the cost of the transmission of water to the Wholesale Customers there shall be two transmission cost pools consisting of an existing transmission cost pool ("Existing Transmission Cost Pool"), and a new transmission cost pool ("New Transmission Cost Pool").
 - a. Existing Transmission Cost Pool. Costs to be allocated to the Existing Transmission Cost Pool shall consist of the following: operation, maintenance, repairs and replacements to the Seattle Transmission Facilities.
 - i. The Seattle Transmission Facilities are owned and operated as a regional network by Seattle to convey water to Wholesale Customers and to Seattle's distribution system. Therefore, the price of transmission for Seattle water transmitted within the Seattle Transmission Facilities shall be calculated on the same basis to holders of Full Requirements Contracts and Partial Requirements Contracts and to Seattle.
 - ii. Costs incurred for purposes of transmission reliability may be included in the Existing Transmission Cost Pool subject to the approval of the Operating Board and Seattle.
 - b. New Transmission Cost Pool. The cost of new transmission facilities shall be included in the New Transmission Cost Pool. The renewal, replacement or modification of existing transmission facilities which create an expansion of transmission capacity may be allocated to the New Transmission Cost Pool. The Operating Board shall decide what portion of costs of renewal, replacement or modification of transmission facilities may be treated as new transmission costs and the portion of the cost of a transmission project that extends the geographic extent of the transmission system that shall be recovered through the New Transmission Cost Pool or from a new Wholesale Customer. Except for costs allocated specifically to a specific Wholesale Customer, New Transmission Cost Pool costs shall be recovered through new transmission rates or FCs. The new transmission rate shall be applied in a uniform manner to all holders of Full Requirements Contracts and Partial Requirements Contracts and Seattle.